Jurisdictional Statement

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No._____

IN THE

SUPREME COURT

OF THE

UNITED STATES

OCTOBER TERM, 1981

STATE OF WASHINGTON, DEPARTMENT OF REVENUE OF THE STATE OF WASHINGTON, and CHARLES W. HODDE, Director of Revenue, and His Successors in Office,

Appellants,

v.

UNITED STATES OF AMERICA,

Appellee.

ON APPEAL FROM THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

JURISDICTIONAL STATEMENT

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QUESTION PRESENTED

Does the Supremacy Clause of the Federal Constitution prohibit a state from imposing a sales or use tax upon a private builder doing business with the federal government under the following circumstances:

(a) All other private builders engaged in a similar business with all other persons, including the state, its agencies and local governments, must pay a sales tax measured by the total contract price, but have the right and obligation under state law to collect that tax as reimbursement from those with whom it is doing business;

(b) Builders doing business with the federal government, on the other hand, have no such right or obligation under state law, but instead must look to the provisions of their contract with the federal government for any reimbursement of the taxes they pay?

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UNITED STATES OF AMERICA,

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OPINIONS BELOW

The opinion of the Court of Appeals for the Ninth Circuit is reported at 654 F.2d 570, and is reproduced as Appendix A hereto. The District Court's order of summary judgment and subsequent amendments thereto are unpublished, and are reproduced as Appendices C through E hereto.

JURISDICTION

This appeal is taken from a judgment of the Court of Appeals for the Ninth Circuit which invalidated, as unconstitutional under the Supremacy Clause, state statutes

which imposed the state retail sales and use taxes upon private builders doing business with the federal government. The judgment of the Court of Appeals affirmed the judgment of the District Court for the Western District of Washington which had likewise invalidated these taxes, on the same grounds, and had enjoined their imposition and collection. Jurisdiction of the District Court was conferred by 28 U.S.C. §1345, and jurisdiction of the Court of Appeals was conferred by 28 U.S.C. §1291.

The judgment of the Court of Appeals was entered on August 24, 1981, and the notice of appeal was filed in that court on November 16, 1981. That notice of appeal is reproduced as Appendix F hereto. Jurisdiction is conferred upon this Court by 28 U.S.C. §1254(2).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

Supremacy Clause (Art. VI, cl. 2) of the United States Constitution.

Revised Code of Washington, §§ 82.04.050, 82.04.190 82.04.280(7), 82.08.020, 82.08.050, 82.12.010, and 82.12.020.

These constitutional and statutory provisions are reproduced as Appendices G-H hereto.

STATEMENT OF THE CASE

A. Washington's Statutory System.

Before 1975, building and other construction work for the federal government were virtually immune from any state sales or use taxes. This situation resulted from the interplay between federal and state law.

Under state law as it existed before 1975, the definition of retail sale included the total charges made by a builder to the property owner. To illustrate: If the total charge for the building was, *e.g.*, $1,000,000, the retail sales tax would apply to that total $1,000,000. Sales to the builder by his suppliers of materials to be incorporated into that building, accordingly, were considered as wholesale sales, and as such exempt from the retail sales tax.

Moreover, state law provided then, as now, that the incidence of the tax was upon the retail buyer, *i.e.*, the property owner. For the seller, *i.e.*, the builder, was required to add the sales tax to the contract price, collect it from the buyer, and pay it over to the state. If the seller did not do so, the state could utilize its collection procedures against the seller; but the seller, in turn, would have a right of action against the buyer for the amount of the tax. Hence, when the buyer was the federal government, no sales tax would be collected either on sales of materials to the builder — because there were wholesale sales — or on the sale by the builder to the federal government — because the federal government was constitutionally immune from the tax.

There were two exceptions to the statutory pattern we have just described. If the building project were a public road, to be owned by the United States or a political subdivision, such as a city or county, the retail sales tax was imposed on the sale of materials to the builder, not on the charge for the total project which the builder made to the public body. To illustrate: If the total contract price for the road were again $1,000,000, and this figure broke down into $500,000 for material costs and $500,000 for labor costs and any profit, the tax would be imposed only on the $500,000 of material costs.

This first exception, for public road projects, did not apply, however, if the road was to be built for the state itself. State road projects were treated in the same manner as other building projects, and accordingly, the tax would be imposed on the total price, *e.g.*, the $1,000,000.

The second exception involved city and county housing authorities. By reason of their statutory exemption from all state sales and use taxes, they were in the same position as the United States; no sales or use tax would be paid on the building project at any stage.

Against this background, the effect of the 1975 statutory changes which precipitated this litigation can be readily understood. Builders for the federal government were put in the same position as public road builders. And so

were builders for city and state housing authorities.[1]

Thus, sales of materials to these two types of builders were made retail sales, whereas previously they had been wholesale sales. The upshot is that, by reason of the 1975 amendments, every single building project results in some sales or use tax revenue for the state. For every project now falls into one or the other of two categories. In the first category are federal building projects, public road projects (except when the state owns the road), and housing authority projects. In the second category are all other building projects.

The tax base for projects in the first category is, of course, smaller than that for projects in the second. The first tax base covers only costs of materials, while the second covers the total contract price, including costs of materials, labor costs, and profit. To use once again our example of a $1,000,000 project, with half that amount being the costs of materials: If that project is in the first category, it generates only half the revenue that would be generated were the project in the second.

The 1975 amendments, in short, placed federal projects in the first category, and thereby removed the complete immunity from taxation which they had previously enjoyed. Because of this effect, the amendments were held to be discriminatory and therefore unconstitutional by the Court of Appeals.

Two final points regarding these amendments. Their effective date was July 1, 1975; however, they were expressly made inapplicable to contracts entered into before that date, or entered into after that date if awarded pursuant to a bid submitted before that date. Further, for contracts not so excluded from the scope of the 1975 amendments, the United States and the builders agreed

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[1]The rather complex technical changes which accomplished this result are fully and accurately described in the opinion of the Court of Appeals (App. A-5-6). As there pointed out, the changes were basically accomplished by amending the definition of "consumer" in Wash. Rev. Code § 82.04.190, to include in that definition prime contractors with the federal government and housing authorities, and to exclude from that same definition the federal government and the housing authorities themselves (see App. A-5, note 6).

that the United States would bear the cost of the taxes if the amendments were upheld, and would receive the refunds required if the amendments were held invalid.

B. The Rationale of the Decision Below.

The Court of Appeals held that the sales and use tax on builders for the federal government was discriminatory, and therefore unconstitutional. As the court viewed it, the discrimination arose because builders for other entities, i.e., for other buyers, were not so taxed. Nor, in the court's view, would that discrimination be removed by reason of the imposition of the sales and use tax on those other buyers themselves, unless it could be shown that the economic incidence of these taxes on those other buyers would necessarily be shifted to their builders.[2] In the absence of such a showing, the imposition of the tax on these other buyers was legally irrelevant.

Nor was it relevant that builders for the federal government might relieve themselves of their tax burden by shifting it to the federal government. As stated by the court:

> "Although it is true that the State's scheme might have the effect of forcing the federal government to reimburse its contractors for the amount of the taxes that they must pay to the State, burdening the federal government in a fashion equivalent to other purchasers of construction work in the State does not make the tax constitutional. The challenged statutes cannot be made valid by equalizing the tax burden of the United States with that of non-federal owners of real property on which construction work is done because a tax either directly imposed on the federal government or indirectly passed on to it be [sic] contractors would be constitutionally impermissible as a tax on the United States without its consent. *See McCulloch v. Maryland,* 17 U.S. (4 Wheat.) 316, 4 L.Ed. 579 (1819). In the absence of the challenged statutes, the United States indeed may be less financially burdened than others who contract with construction contractors, but this advantage constitutionally may *neither* be eliminated by

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[2]We agree with the court that no such showing was made.

> directly taxing the federal government *nor* by taxing those who contract with the federal government while not taxing those 'similarly situated' who contract with others." (App. A, 14; emphasis in original).

The court thus fashioned for the state a legal "Catch 22". Either the tax was shifted to the federal government or it was not. If it was not shifted, the tax was discriminatory; if it was shifted, then it violated the federal government's immunity from taxation established in *McCulloch v. Maryland.*

C. Record Identification of the Question Presented.

The question presented in this appeal was first raised in the Complaint of the United States, filed Feburary 11, 1976, seeking a declaratory judgment invalidating those state statutory provisions which imposed the retail sales and use taxes upon private builders doing business with the federal government. This complaint also sought an injunction against the imposition and collection of these taxes. The grounds asserted for the invalidity of the tax were two-fold; the incidence of the taxes, it was asserted, fell upon the United States, and thus contravened the Federal Constitution (Complaint, Par. 15(a)); and the taxes "discriminate against the United States and its contractors in violation of the Federal Constitution" (Complaint, Par. 15(b)).

The District Court, upon cross-motions for summary judgment, invalidated the taxes on the second ground, but refused to invalidate them on the first. (See Order on Cross Motions for Summary Judgment, Pars. 1-5, Appendix C hereto).

Upon appeal by the State to the Court of Appeals, the Brief of the Appellants raised the question at page 1, under the heading "Statement of the Issues". The Court of Appeals, in affirming the District Court, resolved the question adversely to the State.

THE FEDERAL QUESTION IS SUBSTANTIAL

The federal question is substantial and merits the

noting of probable jurisdiction for two reasons. First, the decision of the Court of Appeals for the 9th Circuit is in irreconcilable conflict with the decision of the three-judge district court in *United States and Olin Mathieson Chemical Corp. v. Illinois Department of Revenue*, 202 F.Supp. 757 (ND Ill. 1962), aff'd *per curiam* 371 U.S. 21 (1962). The confusion arising from this conflict will only be compounded, not diminished, by a *per curiam* affirmance of the Court of Appeals in this case.

Secondly, the resolution of this conflict will necessarily involve an important determination of the scope of this Court's decision in *United States v. County of Fresno*, 429 U.S. 452 (1977), the leading case in this area of the law. This determination will, in turn, resolve an issue of great practical importance to all the states, *i.e.*, the extent to which the United States may utilize its constitutional immunity from state and local taxation to gain an economic advantage in competing, as a purchaser of goods and services in the private sector of the economy, with other purchasers of similar goods and services who enjoy no such immunity.

We briefly take up each of these two points.

I. The Decision of the Court of Appeals is in Irreconcilable Conflict with the Decision in United States and Olin Mathieson Chemical Corp. v. Illinois Department of Revenue, 202 F.Supp. 75 (ND Ill. 1962), aff'd per curiam 371 U.S. 21 (1962).

The question here presented has arisen in the context of a purchase of construction services by the federal government. But it could easily arise in the context of the purchase of anything else, from airplanes to xylophones. This is best demonstrated by *Olin Mathieson* case itself.

At issue in *Olin Mathieson* was the validity of the Illinois retailers occupation tax to sales of aircraft engine starter cartridges by Olin Mathieson to the U.S. Air Force. (202 F.Supp. at 761). By its terms, this tax was imposed only upon the seller. But Illinois law also imposed upon the *purchaser* the traditional type of use tax, equal in

amount to the retailer's occupation tax. And the seller was required to collect that use tax from the buyer.

In order to prevent both taxes from applying to the same transaction, the retailer who paid the occupation tax to the state was allowed to keep the use tax which he had collected from the buyer.

The use tax, of course, could not be imposed upon the Air Force. But could the retailers occupation tax, nevertheless, be imposed upon Olin Mathieson? Illinois took the position that it could. The court described the state's legal position by quoting the applicable Illinois Revenue Rule:

> " 'Since the State cannot place the legal burden of a tax directly on the Federal Government or a foreign government, such governments are not required to remit the use tax directly to this State, nor can such governments be compelled to reimburse retailers for the use tax. However, this does not relieve retailers of their liability for retailers' occupation tax on receipts from retail sales to the Federal Government or to foreign governments * * *' " 202 F.Supp. at 780.

The United States and Olin Mathieson Corp. contended that such a result was discriminatory:

> "The tax which the federal government has here assumed by contract is the tax obligation due the State of Illinois from Olin Mathieson, the retailer. Plaintiffs' argument on discrimination concedes that the use tax is not exacted from the federal government and it is urged by plaintiffs that a retailer who sells to the federal government must pay the occupation tax out of his own pocket because he cannot collect the use tax from the purchasing sovereign; whereas a retailer dealing with a purchaser who is not the federal government need not pay the occupation tax when he collects the use tax from such purchaser." (Emphasis supplied)[3] 202 F.Supp. at 760.

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[3]As we have already noted, at p. 7, *supra*, technically under the Illinois system a retailer dealing with a non-federal purchaser does pay the occuaption tax. But when he collects the use tax, he just pockets it. And the result is exactly the same as if he didn't pay the occupation tax at all, but instead remitted the use tax to the state. And the discrimination argument of the United States in *Olin Mathieson* focused on this practical result.

The court immediately went on to make very short shrift of this argument:

> "* * * This contention of 'discrimination' among retailers because of the immunity of the United States from taxation contradicts the theory urged by plaintiffs. A discrimination among taxpayers resulting from adherence to the doctrine of sovereign immunity is not only reasonable by mandatory." 202 F.Supp. at 760.

This reasoning is completely contrary to that of the Court of Appeals in the case at bar; and the result is as well. Under *Olin Mathieson*, a sales tax — the retailers occupation tax — may be imposed upon a seller to the federal government, and the seller may obtain reimbursement for that tax only if his contract with the federal government so provides. In the absence of such a contract provision, the seller must "pay the * * * tax out of his own pocket", to use the words of the court. All other sellers, on the other hand, have a statutory right to be reimbursed and made whole by their non-federal buyers through the statutory requirement of collection by the buyer of the use tax imposed on the seller.

The only difference, other than nomenclature, between the Illinois system involved in *Olin Mathieson* and the system involved here is that under the Washington system the tax imposed upon the seller to the federal government is less than that imposed upon the non-federal purchaser, because of the smaller tax base. (Cf. p. 4, *supra*)

The conflict between *Olin Mathieson* and the decision of the Court of Appeals is irreconcilable. We must examine next the important practical consequences, to both the States and the federal government, which flow from the manner in which this conflict is resolved.[4]

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[4] *Olin Mathieson* actually dealt with two distinct claims of discrimination against sellers to the federal government. The first is discussed at 202 F.Supp. at 758, 759; the second is discussed at 202 F.Supp. at 759, 760. Our focus here has been on the second. But a comment about the first may be helpful. This first claim arose from the fact that sales to charitable, religious, and educational organizations were exempt from the Illinois retailers occupation tax, and the organizations themselves

II. How the Conflict Between the Decision of the Court of Appeals and the Decision in Olin Mathieson is Resolved Will Determine the Extent to Which the United States May Utilize its Constitutional Immunity from Taxation to Gain an Economic Advantage in Competing, as a Purchaser of Goods and Services in the Private Sector, with Other Purchasers of Similar Goods and Services.

The practical consequences stemming from the manner in which this conflict is resolved can be shown very simply. Under *Olin Mathieson*, a seller of goods or services to the federal government may have to bear the economic burden of a tax which sellers of similar goods or services do not have to bear. This result would be produced by two factors operating in combination: the first factor would be the decision of the federal government not to reimburse its seller for that burden; and the second factor would be the requirement of State law that all other buyers *must* relieve their sellers of that tax burden, by paying that tax to their sellers, who in turn remit it to the State.[8]

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were likewise exempt from the use tax. The Illinois system did not cover these transactions at all; and this prompted a dissent from one of the three district court judges. 202 F.Supp. 760-763. A similar issue, involving the adequacy of the size and composition of the class, also concerned Justice Stevens in his dissent in *United States v. County of Fresno*, 429 U.S. at 471, 472, and Justice White in his dissent in *United States v. Montana*, 440 U.S. at 168, 170. No such issue is presented in this case, however. For under our submission, there is no discrimination against builders doing business with the federal government, *as compared with each and every other builder doing business with all other persons, without exception.* For the Washington system covers them all. The only question is whether the statutory differences in the manner they are covered result in an unconstitutional discrimination.

[8]The upholding of the tax in *Olin Mathieson* did not turn, we suggest, on the fact that the federal government had actually agreed, by contract, to reimburse its seller the amount of the tax imposed upon that seller. Although the District Court mentioned this fact (202 F.Supp. at 760), it did not indicate that this fact was in any way determinative in resolving the discrimination issue. Similarly, the Court of Appeals did not in any way indicate that the presence or absence of any actual reimbursement was determinative. On this point, the two courts are in agreement — and we agree with both. Just as in *Olin Mathieson*, the validity of the state tax here should not turn on whether the federal government has *in fact* agreed to reimburse the tax.

It was exactly this possibility of disparity in economic burdens which concerned the Court of Appeals in the case at bar, and led the Court to strike down the Washington tax. (See App. A-11, 12.)

Yet exactly this same type of disparity would occur under the Illinois tax system, which was upheld in *Olin Mathieson*. But it would occur only to the extent that the federal government decided to let it occur, by choosing not to reimburse the seller, but to pocket the money instead and thereby keep the economic benefit of its own immunity. Under *Olin Mathieson* it is not unconstitutional for a State's tax system to put the federal government to that choice; under the Court of Appeals decision, it *is* unconstitutional.

If, contrary to *Olin Mathieson*, the States cannot put the federal government to that choice, the federal government has a significant economic advantage enjoyed by no other buyers of goods and services in the private sector. It can avoid the economic impact even of those taxes which the State might attempt to place upon its sellers. The taxes which every other buyer must pay can in effect be pocketed by the federal government, as it competes with those buyers in the private marketplace. Or, alternatively, the federal government can share some of the economic benefit of the tax exemption with its sellers, and thereby outbid those other buyers competing for the same goods and services from the same sellers.

Is such an economic advantage constitutionally secured to the federal government? A negative answer to this question, we believe, is required by the Court's decision in *United States v. County of Fresno*, 429 U.S. 452 (1977), in which the Court made a searching re-examination of the basis for the constitutional doctrine that a state may not impose a discriminatory tax upon those doing business with the federal government.

Involved in *Fresno* was the validity of a property tax imposed upon the possessory interests of U.S. Forest Service employees living in federally owned housing supplied to them by the Forest Service as part of their compensation. While tenants holding possessory interests

in privately owned housing were not subject to this same tax, the Court noted that the private landlord himself was required to pay a property tax upon his fee interest in the housing, which was passed onto the tenant in the form of rent. Viewing the California property tax system as a whole, the Court held that the tax on the possessory interests of the Forest Service employees did not interfere with a federal function, provided a sufficient political check against the abuse of the taxing power as applied to these employees, and therefore was not discriminatory against them.

Of special importance, for our purposes, is the practical effect of this decision. As stated in the Court's opinion:

> "The Forest Service fixed the amount of the deduction [for rent] by estimating the fair rental value of a similar house in the private sector and then discounting that figure to take account of the distance between the Forest Service house and the nearest established community and the absence of any customary amenities in or near the house." 429 U.S. at 454.

Since the fair rental value of a similar house in the private sector already had built into it a property tax component, then the result was, as observed by Justice Stevens in his dissent, that the Forest Service employee bore a *heavier* tax burden than the tenant in the private sector; for he had the burden of the additional tax imposed directly on his possessory interest. 429 U.S. at 469 (Justice Stevens dissenting).

The answer of the Court to this problem seems to be, in essence: "That's a problem for the federal government to worry about; it can eliminate it if it so chooses."

For the Court's opinion states:

> "The tax threatens to interfere with federal laws relating to the functions of the Forest Service *only* insofar as it may impose an economic burden on the Forest Service — causing it to reimburse its employees for the taxes legally owed by them or, failing reimbursement, removing an advantage otherwise enjoyed by the Federal Government in the employment market.[12] There is no other respect in which the tax

> involved in this case threatens to obstruct or burden a federal function." 429 U.S. at 464.

And most importantly, footnote 12 states:

> "The Federal Government would otherwise have had the power — enjoyed by no other employer — of giving its employees housing on which no property tax is paid by them either directly or indirectly as rent paid to a landlord who himself paid a property tax."

These passages, especially footnote 12, clearly show that the competitive advantage enjoyed by the federal government by reason of its tax immunity is, in contrast with the immunity itself, not something which merits constitutional protection. And for this reason, the federal government *can* be put to the type of choice to which it is put by the Washington taxing system involved in this case, and by the Illinois taxing system upheld in *Olin Mathieson*. Indeed, as shown by the facts in *Fresno*, the result of the *Fresno* decision was to put the federal government to exactly this same type of choice.[6]

In short, this appeal involves an important application of this Court's decision in *Fresno*. The proper application of that decision will, in turn, resolve the conflict between the Court of Appeals in this case and the decision in *Olin Mathieson*. And the practical consequences of how that conflict is resolved are of great nationwide importance, whether a property tax system is involved, as in *Fresno*, or a sales and use tax system, as in *Olin Mathieson* and as here.

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[6] The Court of Appeals, obviously, did not read *Fresno* this broadly. Instead, it read *Fresno* as requiring the State to show that non-federal buyers actually passed the economic burden of the sales and use taxes back to their sellers. This is entirely too narrow a reading of *Fresno*; for it completely overlooks this Court's treatment of the federal government's competitive advantage which it derives from its constitutional immunity from taxation.

CONCLUSION

For the reasons given above, probable jurisdiction should be noted, and the decision of the Court of Appeals reversed.

DATED this 20th day of November, 1981.

Respectfully submitted,

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APPENDIX A

[Filed and entered August 24, 1981]

UNITED STATES of AMERICA,
Plaintiff-Appellee,

v.

STATE OF WASHINGTON; Department of Revenue of the State of Washington; and Charles W. Hodde, Director of Revenue, and his successors in office, Defendants-Appellants.

No. 78-1424.

UNITED STATES COURT OF APPEALS,
NINTH CIRCUIT.

Argued and Submitted May 7, 1980.

Decided Aug. 24, 1981.

Federal Government brought action challenging Washington sales and use tax statutes. The United States District Court for the Western District of Washington, Donald S. Voorhees, J., entered judgment in favor of Federal Government and State appealed. The Court of Appeals, Wm. Matthew Byrne, Jr., District Judge for the Central District of California, sitting by designation, held that Washington sales and use tax statutes imposing taxes on contractors dealing with the Federal Government were unconstitutional.

Affirmed.

1. Taxation—1207

Mere differential treatment of those contractors dealing with the federal government does not in itself render a sales or use tax invalid.

2. Taxation—1207

Where no contractors except those dealing with the United States are taxed or necessarily have another's tax

burden economically shifted to them under the Washington sales and use tax, federal contractors were financially disadvantaged in a way which had constitutionally impermissible potential of interfering with the functions of the federal government. U.S.C.A. Const. Art. 6, cl. 2.

3. Taxation—1207

If a tax treats those dealing with the government in a more disadvantageous fashion than those not dealing with it, the potential for interfering with the functioning of the federal government has been unconstitutionally created. U.S.C.A. Const. Art. 6, cl. 2.

4. Taxation—1207

Fact that the federal government might be less financially burdened than others who contracted with construction contractors was an advantage which constitutionally could not be eliminated directly by taxing the federal government nor by taxing those who contract with federal government while not taking those similarly situated who contract with others.

5. Taxation—1207

Tax may be imposed upon those who deal with the federal government only if burden of the tax is equally felt by those similarly situated who do not deal with the federal government.

6. Taxation—1207

Provisions of Washington's sales and use tax which imposed sales tax on items bought by contractors for incorporation in federal project, while not imposing that tax on contractor's making purchases for incorporation in other projects for other parties, were unconstitutional. West's RCWA 82.04.010 et seq., 82.08.010 et seq., 82.14.010

et seq.; U.S.C.A. Const. Art. 6, cl. 2.

On Appeal from the United States District Court for the Western District of Washington.

Before ANDERSON and SKOPIL, Circuit Judges, and BYRNE,* District Judge.

WM. MATTHEW BYRNE, JR., District Judge:

This appeal is from an order of the district court, which declared unconstitutional three 1975 sales and use tax statutes of the State of Washington (the "State") insofar as those statutes imposed such taxes on prime contractors for construction activity performed on federally-owned land. The district court's order also permanently enjoined the State from assessing or collecting the challenged taxes and directed the State to refund such taxes as had been theretofore collected.

The primary issue presented in this appeal is whether the challenged tax statutes unconstitutionally discriminate against those with whom the United States deals, in violation of the Supremacy Clause of the United States Constitution.[1] This issue requires application of the principles enunciated in the long line of cases from *McCulloch. v. Maryland*, 17 U.S. (4 Wheat.) 316, 4 L.Ed. 579 (1819), through, most recently, *United States v. County of Fresno*, 429 U.S. 452, 97 S.Ct. 699, 50 L.Ed.2d 683 (1977).

I. *THE CHALLENGED TAXES*

Pursuant to Chapters 82.04, 82.08 and 82.14 of the Revised Code of Washington, the State assesses and collects a "sales" tax on every retail sale of tangible personal property within the State. Pursuant to Chapters 82.12 and 82.14 thereof, a "use" tax is similarly assessed

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*The Honorable Wm. Matthew Byrne, Jr., United States District Judge for the Central District of California, sitting by designation.

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[1] "This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; * * * *" U.S. Const. art. VI, cl 2.

and collected on certain specified consumer uses of such property within the State.[2] These taxes are imposed on the "consumer" or "buyer" of the property, terms that are quite broadly defined by Wash. Rev. Code §§ 82.04.190 and 82.08.010. Prior to July 1, 1975, the statutes in question defined the terms "retail sale," "consumer," and "buyer" in such a way that no sales or use tax was imposed on any prime contractor or subcontractor with respect to the purchase or use of personal property, if such property was to be incorporated into a construction project.[3] As a result of the definitions of these terms, the contract between the prime contractor and the owner of the realty became the only taxable "retail sale" of the construction project or of any personal property incorporated therein. The owner of the realty[4] was thus statutorily defined as

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[2]The general State retail sales tax has fluctuated between 4.5 and 4.6 percent of the "selling price." Wash. Rev. Code § 82.08.020. The general State use tax has similarly fluctuated between 4.5 and 4.6 percent of the "value of the article used." Wash. Rev. Code § 82.12.020.

The challenged tax statutes also authorize local counties and municipalities to assess and collect comparable sales and use taxes. Local sales and use taxes have ranged from zero to 0.8 percent of the selling price (in the case of a sales tax) or value of the article used (in the case of a use tax), depending upon the local governments with jurisdiction, with a statutory maximum of 0.925 percent. Wash. Rev. Code §§ 82.14.030 and 82.14.045.

[3]For example, Wash. Rev. Code § 82.04.190(1)(b) at the time defined "Consumer," in part, to include:

> (1) Any person who purchases, acquires, owns, holds, or uses any article of tangible personal property irrespective of the nature of his business and including, among others, without limiting the scope hereof, persons who install, repair, clean, alter, improve, construct, or decorate real or personal property of or for consumers *other than* for the purpose * * * (b) of incorporating such property as an ingredient or component of real or personal property when installing, repairing, cleaning, altering, imprinting, improving, constructing or decorating such real or personal property of or for consumers * * * * [emphasis added].

[4]Throughout this opinion, as a matter of convenience, we shall refer to the entity with whom the prime contractor contracts as the "owner" of the realty. It is important to recognize, however, that the taxes are not limited to only such consumers. Under Wash. Rev. Code § 82.04.190(4), a consumer, upon whom the taxes are imposed, includes any person "who is an owner, lessee or has the right of possession to or an easement in real property which is being constructed, repaired, decorated, improved or otherwise altered by a person engaged in a business * * * *"

the only "consumer" or "buyer" and was, therefore, the only one directly liable for the sales or use taxes imposed. These taxes were collected from the owner of the realty by the prime contractor for eventual payment to the State.

Under the tax scheme described above, no sales or use tax was imposed with regard to construction projects or material incorporated into construction projects on real property owned by the United States or an instrumentality thereof. The State has conceded that any tax levied directly upon the federal government's own acquisition or use of personal property within the State would have violated the Supremacy Clause, which grants to the United States and its instrumentalities complete immunity from state taxes, unless the federal government consents to such taxes.[5]

Effective July 1, 1975, the State amended the above statutes, so that, with respect to construction on *federally*-owned land, the prime contractor came to be treated as the "consumer" or "buyer," and thus became directly liable for the State's sales and use taxes on materials it acquired or was furnished for incorporation into such federal projects.[6]

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[5]*See Diamond Nat'l Corp. v. State Bd. of Equalization*, 425 U.S. 268, 96 S.Ct. 1530, 47 L.Ed.2d 780 (1976); *United States v. Mississippi Tax Comm'n*, 421 U.S. 599, 95 S.Ct. 1872, 44 L.Ed.2d 404 (1975); *First Agricultural Nat'l Bank v. State Tax Comm'n*, 392 U.S. 339, 88 S.Ct. 2173, 20 L.Ed.2d 1138 (1968); *Kern-Limerick, Inc. v. Scurlock*, 347 U.S. 110, 74 S.Ct. 403, 98 L.Ed. 546 (1954); *McCulloch v. Maryland*, 17 U.S. (4 Wheat.) 316, 4 L.Ed. 579 (1819).

[6]The manner in which this was accomplished is somewhat complex. The change was effected by substitute House Bill No. 86, enacted into law as Chapter 90, Laws of 1975 (amending Wash. Rev. Code §§ 82.04.050 and 82.04.190); Section 5 of Substitute House Bill No. 2736, enacted into law as Section 5 of Chapter 291, Laws of 1975 (amending Wash. Rev. Code § 82.04.050) and House Bill No. 1229, enacted into law as Chapter 1, Laws of 1975-76 (amending Wash. Rev. Code §§ 82.12.010 and 82.12.020). These statutes added the following definition of "consumer" to Wash. Rev. Code § 82.04.190:

> "Consumer" means the following: * * *
>
> (6) Any person engaged in the business of constructing, repairing, decorating, or improving new or existing buildings or other structures under, upon or above real property of or for the United States, any instrumentality thereof, or a county or city housing authority created pursuant to chapter 35.82 RCW, including the installing or attaching of any article of tangible personal property

However, prime contractors on non-federal projects, other than local housing authority projects,[7] continued not to be treated as "consumers" and paid no tax on their purchase or use of materials incorporated into such projects.

II. *PROCEDURAL BACKGROUND*

The United States filed its original complaint on February 16, 1976 against the State, the Department of Revenue of the State, and Mary Ellen McCaffree, Director of Revenue of the State, and her successors in interest (the "Defendants"). The complaint sought: (1) a declaratory judgment that the Washington Sales and Use Tax Act, Chapters 82.08, 82.12 and 82.14, Revised Code of Washington, as amended, as applied to construction activity involving the United States within the State, was unconstitutional under the Supremacy Clause; (2) a permanent injunction against the State imposing, assessing or collecting such taxes; and (3) an order directing the refund of such taxes as had been collected, with appropriate inter-

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therein or thereto, whether or not such personal property becomes a part of the realty by virtue of installation. Any such person shall be a consumer within the meaning of this subsection in respect to tangible personal property incorporated into, installed in, or attached to such building or other structure by such person.

These statutes further expressly excluded from the definition of "consumer" "the United States, instrumentalities thereof, and county and city housing authorities created pursuant to chapter 35.82 RCW in respect to labor and services rendered to their real property." Wash. Rev. Code § 82.04.190(4). Wash. Rev. Code § 82.04.050 was also amended so as to redefine "retail sale" and "sale at retail" to *exclude* expressly from their scope contracts calling for the improvement, repair or construction of real property owned by the United States or any of its instrumentalities and to *include* sales of materials to prime contractors engaged in construction work on federally-owned property. As with the sales tax, the liability of federal prime construction contractors for the State's use tax arose basically from the inclusion of such contractors within the meaning of the term "consumer," and the use of that term in Wash. Rev. Code § 82.12.020, under which the use tax is levied.

[7]The constitutionality of imposing these taxes on private contractors dealing with local housing authorities is not presented in this appeal. It is, however, discussed, although not reached (because of the jurisdictional bar of the Johnson Act, 28 U.S.C. § 1341), in the related case of *Housing Authority v. State of Washington*, 629 F.2d 1307 (9th Cir. 1980).

est.[8] After all Defendants answered, the parties filed cross-motions for summary judgment as to all issues except the precise amount of refund that might be due.[9] Defendants appeal from the district court's order, which amended and supplemented its original order on the cross-motions for summary judgment.

III. *DISCUSSION*

The United States contends, and the district court ruled, that the imposition of the State sales and use taxes upon prime contractors' acquisition and use of tangible personal property for ultimate incorporation into federal construction projects unconstitutionally discriminates against such contractors because prime contractors on non-federal projects are not similarly taxed.

The State concedes the principle that "a tax may be invalid even though it does not fall directly on the United States if it operates so as to discriminate against the Government or those with whom it deals." *United States v. City of Detroit*, 355 U.S. 466, 473, 78 S.Ct. 474, 478, 2 L.Ed.2d 424, 429 (1958). *See also Phillips Chemical Co. v. Dumas Independent School District*, 361 U.S. 376, 80 S.Ct. 474, 4 L.Ed.2d 384 (1960). The State argues, however, that the Supreme Court has recognized that mere disparate treatment of those dealing with the United States is not enough to render a state tax law unconstitutional. The State contends that the district court erred in concluding that there exists in this case the sort of discriminatory taxation against which the Suprem-

[8]The United States is seeking a refund only of those sales and use taxes that have been paid to the State by prime contractors on federal projects and with respect to which those contractors have claimed and received from the United States reimbursement separate and apart from the general contract price.

[9]Because the case has been filed prior to the August 12, 1976 repeal of 28 U.S.C. § 2281 and sought a declaration of the unconstitutionality of a state statute, application was made for a three-judge federal district court to hear the motions. Before the application was acted upon, however, and to avoid the necessity of convening a three-judge district court, the original action was dismissed by stipulation and order of the court and was subsequently refiled, along with all the pleadings then on file, which were all deemed refiled as of May 12, 1977.

acy Clause protects the federal government and those with whom it deals.

The State relies chiefly on *United States v. County of Fresno*, 429 U.S. 452, 97 S.Ct. 699, 50 L.Ed.2d 683 (1977), and *United States v. City of Detroit*, 355 U.S. 466, 78 S.Ct. 474, 2 L.Ed.2d 424 (1958). At issue in *Fresno* was a "possessory interest" tax that the State of California imposed upon renters of housing on tax-exempt real property and not upon renters of housing on taxable real property. The United States Forest Service had furnished housing on federal property to certain of its employees as partial compensation for the services they rendered to the Forest Service. California determined that the employees "rented" the housing they were furnished. Because the housing was on tax-exempt property, California assessed the employees an annual possessory interest tax on the value of their interest in the housing.

The Court held the California tax constitutionally valid. The Court reviewed its line of cases since *McCulloch v. Maryland*, 17 U.S. (4 Wheat.) 316, 4 L.Ed. 579 (1819), and explained that, in *McCulloch*, the Court had rejected Maryland's argument that the State's power to tax the Bank of the United States only involved the impermissible power to destroy the Bank when the State's taxing power was abused, and that the states should be trusted not to abuse their power to tax a federal function just as a state must be trusted not to abuse its power to tax its own citizens. That argument was rejected, according to the *Fresno* court,

> because the political check against abuse of the power to tax a State's constituents is absent when the State taxes only a federal function. A State's constituents can be relied on to vote out of office any legislature that imposes an abusively high tax on them. They cannot be relied upon to be similarly motivated when the tax is instead solely on a federal function. [footnote omitted].

Fresno, 429 U.S. at 458-59, 97 S.Ct. at 703, 50 L.Ed.2d at 689-90.

Reviewing the cases since *McCulloch*, the *Fresno* Court concluded that,

> [s]o long as the tax is not directly laid on the Federal Government, it is valid if nondiscriminatory * * * * The rule to be derived from the Court's more recent decisions * * * is that the economic burden on a federal function of a state tax imposed on those who deal with the Federal Government does not render the tax unconstitutional so long as the tax is imposed equally on the other similarly situated constituents of the State. [citations omitted].

429 U.S. at 460-62, 97 S.Ct. at 704-05, 50 L.Ed.2d at 691-92.

Thus, the Court held that the tax imposed on renters of tax-exempt real property was nondiscriminatory and therefore constitutional, because,

> the State of California imposed a property tax on owners of non-exempt property which is "passed on by them to their * * * lessees." Consequently, the appellants who rent from the Forest Service are no worse off * * * than those who work for private employers and rent houses in the private sector.

429 U.S. at 465, 97 S.Ct. at 706, 50 L.Ed.2d at 694.

Similarly, in *Detroit*, the Supreme Court upheld a Michigan law that imposed on users of tax-exempt property a use tax comparable to the property tax imposed on owners of taxable property. The Court stated that

> here the tax applies to every private party who uses exempt property in Michigan in connection with a business conducted for private gain. Under Michigan law this means persons who use property owned by the Federal Government, the State, its political subdivisions, churches, charitable organizations and a great host of other entities * * * * [T]he legislature apparently was trying to equate the tax burden imposed on private enterprise using exempt property with that carried by similar businesses using taxed property. Those using exempt property are required to pay no greater tax than that placed on private owners or passed on by them to their business lessees. [footnote omitted].

355 U.S. at 473-74, 78 S.Ct. at 478, 2 L.Ed.2d at 429.

The State argues that the factual patterns in *Fresno* and *Detroit* are analogous to that presented in this case. The State urges that both the "renters" of tax-exempt

property in *Fresno*, who constitutionally could be required to pay a tax otherwise imposed upon owners of non-exempt real property, and the users of tax-exempt property in *Detroit*, who constitutionally could be required to pay a tax otherwise imposed upon owners of non-exempt property, are in positions parallel to the contractors of projects on tax-exempt federal realty who, under the challenged statutes, are required to pay taxes otherwise imposed upon owners of non-federal non-exempt realty on which construction work is done.

The State makes three intertwined arguments in constructing this supposed parallel. First, it argues that its taxation scheme, when viewed as a whole, is constitutional because it taxes comparably those who are similarly situated, by imposing the same level of taxation on all "consumers" in the State. In a closely-related argument, the State urges that the political check that the Supreme Court described in *Fresno* as necessary and sufficient to make disparate tax treatment of those dealing with the federal government constitutional is provided through the State's imposition of the same sales and use taxes on a broad base of the State's residents. The State contends that the United States need not fear that its functions will be burdened by abusive taxation of those with whom it deals because a sufficient political check is provided in the State's equal taxation of all its "consumers." Finally, the State argues that, by taxing prime contractors on federal projects at the same rate as owners of realty on which non-federal projects are constructed,[10] it has done no more than properly equalize the financial burden imposed upon all those who contract with construction contractors. In the absence of the challenged statutes, the State submits both that it would lose a significant amount of revenue that otherwise would be due it if the construction work were done on non-federal land and that the United States would

[10]Although the rates are the same, the tax that the contractors are required to pay may be less than the taxpaid by owners of non-federal realty on which construction work is done because the constractors are taxed only on the materials incorporated into the project, whereas the owners pay a tax that includes the cost of labor and services performed by the contractor.

obtain an unfair advantage, relative to other owners of realty on which construction work is done in the State.

Each of the State's arguments significantly misconstrues the Supreme Court's reasoning and language. First, in defining which groups were "similarly situated" for purposes of determining whether treatment of those dealing with the federal government was discriminatory, the *Fresno* Court compared the Forest Service employee "renters" to renters of real property that was not tax-exempt. Although Justice Stevens disagreed, the Court, per Justice White, held that because property owners of taxable real property would pass along the property tax imposed upon them to their renters, all *renters* (both those who "rented" from the federal government and those who did not) were being placed in a similar position. In *Detroit*, the Court likewise reasoned that the tax involved was non-discriminatory because those using tax-exempt property paid the same tax as was passed on by owners of taxed property to their business lessees. The similarly situated group examined was again not all taxpayers, but all *users* of property. In the instant case, therefore, the relevant "similarly situated" group is not all "consumers," as the State suggests, but rather all prime contractors. The State's statutory inclusion of prime contractors of federal projects within its definition of "consumers" does not automatically free the tax from constitutional doubt. What must be examined is whether prime contractors on federal projects are disadvantaged in comparison to prime contractors on non-federal projects.

[1] Although mere *differential* treatment of those contractors dealing with the federal government does not in itself render the tax invalid,[11] the taxation scheme here operates to burden only those prime contractors who work on federal rather than State or private projects. The taxes cannot be justified under the authority of *Fresno* as being

[11]For example, if prime contractors dealing with private enterprises were directly taxed, but prime contractors dealing with the federal government were exempted from such taxes, no constitutional infirmity would be created. It is not differential treatment that is prohibited but, rather, treatment that acts to favor those not dealing with the United States over those dealing with it.

an equalization of the tax burden imposed on non-federal contractors, because non-federal contractors are not taxed directly upon their acquisition of materials for incorporation into the projects upon which they work. Nor is there anything in the record from which to conclude that the economic incidence of the sales and use taxes would necessarily be shifted from the owners of non-federal land to their prime contractors.[12] Therefore, it has not been demonstrated that the tax burdens on all contractors are, in fact, equalized.[13]

[2, 3] Because no contractors except those dealing with the United States are taxed, or necessarily have another's tax burden economically shifted to them, as occurred in *Fresno* and *Detroit*, federal contractors are financially disadvantaged in a way that has the constitutionally impermissible potential of interfering with the functions of the federal government. The State's preferential treatment of prime contractors on non-federal projects could discourage contractors from performing work for the United States or could lead to their doing so only at higher

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[12]In both *Fresno* and *Detroit* the Supreme Court concluded that the economic incidence of the subject taxes would be passed through to those who dealt with the directly taxed sectors. *See* Slip op. pp. 4218-4220, pp. _____-_____ *supra*. In the instant case, there are no findings, economic data, or demonstrated market assumptions in the record from which to conclude that: 1) the owners of non-federal property have sufficient market power vis-a-vis prime contractors to pass on the economic incidence of the subject tax; 2) even if such market power exists generally, why all owners of non-federal property would necessarily have sufficient market power to allow each of them to pass on all of the economic incidence to prime contractors; and 3) even if both of these conclusions are now true, that they will remain so, notwithstanding any changes in economic conditions. *Cf. Fresno*, 429 U.S. at 470, 97 S.Ct. at 708, 50 L.Ed.2d at 697 (Stevens, J., dissenting) ("The private owner's tax obligation is one of the factors that determines the fair rental value * * * but it is not correct to say that the owner's tax is paid by the tenant."); *United States v. California State Bd. of Equalization*, 650 F.2d 1127 at 1132 (9th Cir. 1981) (district court finding that state use tax discriminated against United States and its contractors was vacated as being "totally unsupported by anything in the record").

[13]The Court notes that those contractors not dealing with the United States cannot have their assets levied upon or seized for satisfaction of the tax liability, and need not pay over the tax that they have collected from the owner of the realty until the project is completed and they have been paid in full.

levels of compensation than demanded for comparable non-federal work. We need not determine whether the taxes, by being imposed directly upon a contractor only when the contractor deals with the United States, actually have the effect of interfering with federal functions. As the Supreme Court said in *Fresno* of the decision in *McCulloch v. Maryland*:

> If the State's power to tax * * * were recognized in principle, * * * [it is doubtful whether the federal courts would have the ability] to review each exercise of such power to determine whether the tax would or would not destroy a federal function.

Fresno, 429 U.S. at 458, 97 S.Ct. at 702, 50 L.Ed.2d at 689. If a tax treats those dealing with the United States in a more disadvantageous fashion than those not dealing with it, as do these taxes, the potential for interfering with the functioning of the federal government has been unconstitutionally created.

As to the State's second related argument, the political check that was described in *Fresno* simply is not present in this case. In *Fresno*, there was a similarly situated group that was analogously taxed, namely, the lessees of non-exempt property. That group provided the necessary political safeguard. Here there is no broad state constituency taxed as are the prime contractors who deal with the federal government. Only when those similarly situated not dealing with the federal government feel the same tax burden as those dealing with it, can the State's constituency be relied upon to ensure that the taxation does not rise to abusive levels. Thus, only if all prime contractors were forced either directly or indirectly to pay the challenged taxes would the political check described in *Fresno* be present. In that situation alone would it be clear that those with interests comparable to federal contractors could be relied upon to ensure that the tax on federal contractors would not rise to abusive levels.[14]

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[14]In this regard, the Court agrees with and takes some guidance from the dissent of Justice White, the author of the majority opinion in *Fresno*, in the recent case of *Montana v. United States*, 440 U.S. 147, 99 S.Ct. 970, 59 L.Ed.2d 210 (1979). Although the majority decided that

[4] The State's final argument, that it has properly equalized the burden imposed on all who contract with construction contractors, is equally misdirected. Although it is true that the State's scheme might have the effect of forcing the federal government to reimburse its contractors for the amount of the taxes that they must pay to the State, burdening the federal government in a fashion equivalent to other purchasers of construction work in the State does not make the tax constitutional. The challenged statutes cannot be made valid by equalizing the tax burden of the United States with that of non-federal owners of real property on which construction work is done because a tax either directly imposed on the federal government or indirectly passed on to it be contractors would be constitutionally impermissible as a tax on the United States without its consent. *See McCulloch v. Maryland,* 17 U.S. (4 Wheat.) 316, 4 L.Ed. 579 (1819). In the absence of the challenged statutes, the United States indeed may be less financially burdened than others who contract with construction contractors, but this advantage constitutionally may *neither* be eliminated by directly taxing the federal government *nor* by taxing those who contract with the federal government while not taxing those "similarly situated" who contract with others.

IV. *CONCLUSION*

[5, 6] A tax may be imposed upon those who deal

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case on grounds of collateral estoppel and did not reach the Supremacy Clause issue, Justice White wrote that he believed that imposition of Montana's one percent gross receipts tax upon contractors of public, but not private, construction projects was unconstitutional. It was not enough, he stated, that the tax was imposed on contractors of state as well as federal projects. 440 U.S. at 172, 99 S.Ct. 983, 59 L.Ed.2d at 229. Rather, he explained, in order to be "imposed equally" upon "similarily situated constituents of the State," the same tax would have to be imposed upon contractors of private construction projects. 440 U.S. at 170-72, 99 S.Ct. at 982-83, 59 L.Ed.2d at 227-28. Only then, he stated, would there be an "efficacious 'political check' on potentially abusive taxation." 440 U.S. at 170, 99 S.Ct. at 982, 59 L.Ed.2d at 228. Similarily, in this case, the only political check that would be constitutionally adequate would be similar taxation of all construction contractors in the State.

with the federal government only if the burden of the tax is equally felt by those "similarly situated" who do not deal with the federal government. The State's statutory scheme places a tax burden on construction contractors dealing with the United States, one which is not placed upon constractors who perform similar work for non-federal owners of real property. The challenged taxes discriminate against those with whom the federal government deals, and have the potential for interfering with the functions of the federal government. They are, therefore, unconstitutional under the Supremacy Clause of the United States Constitution.[15]

Accordingly, the court's order below is AFFIRMED.

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[15]Because we affirm on the basis of the statutes' unconstitutional discrimination against those with whom the United States deals, we need not reach the issues presented by the alternative ground of possible unconstitutionality, which was urged by the United States below but rejected by the district court, that the legal incidence of the taxes unconstitutionally falls upon the United States. *Cf. United States v. California State Bd. of Equalization*, 650 F.2d 1127 at 1131 (9th Cir. 1981) (where there is a "strong economic incentive" that "all but compels" the lessor to collect a sales tax from the lessee, coupled with a legislative intent that lessee pay the tax, the legal incidence thereof is unconstitutionally placed on lessee-United States).

APPENDIX B

No. 78-1424
DC CV 77-355 DSV

IN THE

UNITED STATES COURT OF APPEALS

FOR THE
NINTH CIRCUIT

UNITED STATES OF AMERICA,
Plaintiff-Appellee,

VS.

STATE OF WASHINGTON; DEPARTMENT OF REVENUE OF THE STATE OF WASHINGTON, et al.,
Defendants-Appellants.

APPEAL from the United States District Court for the WESTERN District of WASHINGTON (Seattle).

THIS CAUSE came on to be heard on the Transcript of the Record from the United States District Court for the WESTERN District of WASHINGTON (Seattle) and was duly submitted.

ON CONSIDERATION WHEREOF, It is now here ordered and adjudged by this Court, that the judgment of the said District Court in this Cause be, and hereby is affirmed.

Filed and entered August 24, 1981.

APPENDIX C

No. C77-355V

IN THE

UNITED STATES DISTRICT COURT

FOR THE

WESTERN DISTRICT OF WASHINGTON

UNITED STATES OF AMERICA,

Plaintiff,

vs.

STATE OF WASHINGTON; et al.,

Defendants.

ORDER ON CROSS-MOTIONS FOR SUMMARY JUDGMENT

Having considered plaintiff's motion for partial summary judgment and defendants' cross-motion for summary judgment of dismissal, together with the memoranda, affidavits and other materials submitted by counsel, the Court now finds and rules as follows:

1. The Court finds that the provisions of RCW 82.04, 82.08, 82.12 and 82.14 as applied by the State of Washington to impose a sales tax on contractors who acquire materials for incorporation into federal construction projects, unlawfully discriminates against contractors who deal with the United States and that this discrimination is in violation of the Supremacy Clause of the United States Constitution. A state may lawfully impose a sales tax upon private contractors who purchase property in that state for incorporation into a federal project but only if it imposes a sales tax upon contractors who purchase such materials for incorporation into projects

other than federal ones. This Court finds that the tax imposed on federal project contractors by the defendants' dual scheme of construction project taxation imposed a burden of taxation upon those contractors which is not similarly imposed upon non-federal project contractors and that the tax is therefore impermissibly discriminatory.

2. The Court further finds that the sales tax on materials purchased for incorporation into federal projects cannot be justified, under the authority of *United States v. Fresno*, 50 L.Ed.2d 683 (1977), as being an equalization of the tax burden imposed upon non-federal project contractors. Contractors on state or private construction projects in this state, unlike federal project contractors, are not taxed directly or indirectly upon their acquisition of materials for incorporation into the projects upon which they work. In consequence the imposition of a sales tax upon federal project contractors cannot be an equalization of the tax burden between federal and non-federal contractors.

3. The Court further finds that this statutory scheme also imposes an unlawfully discriminatory tax upon the use by federal contractors of materials furnished to them by the United States for incorporation into federal construction projects. As with the sales tax, this use tax is not an equalization of the tax burden imposed on contractors who work on federal projects with the burden imposed upon those who work upon non-federal projects. The invalidation of this use tax will not cause federal contractors to have an unfair economic advantage over non-federal contractors.

4. The Court finds, however, that the imposition of use taxes upon materials furnished by the United States to federal project contractors for use in connection with those projects but not for incorporation into those projects does not result in any constitutionally impermissible discrimination against federal project contractors, inasmuch as that same use tax is imposed upon contractors working on state or private projects. The imposition of this tax upon federal project contractors does not in consequence result in any discrimination against those who contract with the

United States.

5. The Court finds that the legal incidence of all three of the challenged taxes falls upon the contractors and not upon the United States. A non-discriminatory imposition of these taxes upon federal project contractors would not threaten or interfere with any function of the United States except insofar as it might indirectly burden the United States with a contractual duty to reimburse the contractors for taxes which they have been required by the state to pay. See: *United States v. Fresno*, 50 L.Ed.2d 683 (1977).

Accordingly, it is hereby adjudged and declared that the provisions of RCW 82.04, 82.08, 82.12 and 82.14, as applied by the State of Washington to impose a sales tax on federal project contractors who acquire materials for incorporation into federal projects and as applied to impose a use tax upon the use by federal project contractors of materials furnished by the United States for incorporation into those projects, unlawfully discriminates against those who deal with the United States in violation of the Supremacy Clause of the United States Constitution.

Accordingly, defendants are ENJOINED from assessing or collecting either of these invalid taxes.

It is further ORDERED that defendants repay the sale and use taxes which have been impermissibly collected.

Counsel for plaintiff and defendants are directed to meet and to endeavor to determine the amount of taxes to be refunded. Counsel shall report back to the Court within 60 days of this order. In the event the parties are unable to agree on the amount of taxes to be refunded, this Court will at that time consider the appointment of a special master to make that determination.

The Clerk of this Court is instructed to send uncertified copies of this order to all counsel of record.

DATED this 3rd day of November, 1977.

/s/ Donald S. Voorhees

UNITED STATES DISTRICT JUDGE

APPENDIX D

No. C77-355V

IN THE

UNITED STATES DISTRICT COURT

FOR THE

WESTERN DISTRICT OF WASHINGTON

UNITED STATES OF AMERICA,

Plaintiff,

v.

STATE OF WASHINGTON, et al.,

Defendants.

ORDER ON AGREED MOTION TO AMEND ORDER ON CROSS-MOTIONS FOR SUMMARY JUDGMENT

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Having considered the agreed motion of the plaintiff and the defendants to amend this Court's order of November 3, 1977, which denied the defendants' motion for summary judgment and granted in part the plaintiff's motion for partial summary judgment, and the Court being fully advised in the premises, it does hereby amend and supplement the order of November 3, 1977, as follows:

ORDERED that the issue as to the amount of the refund of taxes to be made to the United States pursuant to this Court's order of November 3, 1977, is hereby severed for separate trial and trial proceedings from the issues heretofore adjudicated by this Court in its order of November 3, 1977; and it is further

ORDERED that the plaintiff United States of America advise the defendant State of Washington by March 1, 1978, as to those State sales and use taxes to which it claims a refund by virtue of this Court's order of November 3, 1977; and further that in so advising the State as to which monies it claims a refund, the United States shall advise the State of Washington as to the dates and the amounts of any such tax payments for which it claims a refund, together with the persons to whom the United States made such payments; and further that in identifying any such payments for which it claims a refund, the United States shall, if it has such information in its possession, advise the State of Washington as to the identity of any persons who remitted said taxes to the State of Washington, together with the dates and amounts of their remittances; and it is further

ORDERED that the State of Washington shall review the foregoing information submitted to it by the United States of America and conduct such further audits and investigations as it deems necessary to the end that it shall report back to this Court by July 1, 1978, the results of its audits and investigations and shall advise the Court which claims of the United States it will agree to refund and which claims of the United States remain in dispute, at which time this Court will consider what further trial or other proceedings may be necessary; and it is further

ORDERED that in view of the four-year limitation pre-

scribed by RCW 82.32.050 upon the right of the defendants to issue assessments for additional taxes due, and giving due consideration to the security of the rights of the defendants pending the ultimate disposition of this cause by the appellate courts of the United States, the Court acting pursuant to Rule 62(c) of the Federal Rules of Civil Procedure hereby modifies the injunction heretofore entered by the Court on November 3, 1977, as follows: During the pendency of any appeal of the injunction heretofore entered, defendants may issue assessments on the amount of the subject sales and use taxes which would have been due and payable under the challenged State statutes were such statutes constitutionally valid, but only with respect to such otherwise taxable transactions or activities as occurred prior to November 3, 1977, and only if such assessments provide that the date upon which the tax shall be due and payable is 120 days following the rendition of a decision upholding the constitutional validity of the challenged State statutes by the United States Court of Appeals for the Ninth Judicial Circuit, or thereafter by the United States Supreme Court if appeal be had to that Court.

Dated this 30th day of December, 1977.

/s/ Donald S. Voorhees
UNITED STATES DISTRICT JUDGE

Presented by:

/s/ Richard H. Holmquist
Richard H. Holmquist
Senior Assistant Attorney General

APPENDIX E

CIVIL ACTION
No. C77-355V

IN THE

UNITED STATES DISTRICT COURT

FOR THE
WESTERN DISTRICT OF WASHINGTON

UNITED STATES OF AMERICA,

Plaintiff,

vs.

STATE OF WASHINGTON, et al.,

Defendants.

ORDER CONFIRMING AMOUNT AND DIRECTING REFUND OF STATE TAXES

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United States Attorney

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JOHN J. McCARTHY
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SLADE GORTON
Attorney General
State of Washington

LELAND T. JOHNSON
Senior Assistant Attorney General
415 General Admin. Bldg., AX-02
Olympia, WA 98504
(206) 753-5528

This matter having come on for hearing before this court on October 7, 1977 and this court having issued its order on cross-motions for summary judgment on November 3, 1977; and this court having by order of December 30, 1977 amended its previous order of November 3, 1977 to sever the issue of the amount of refund from other issues adjudicated by the court in its order of November 3, 1977, and by further order to extend the time for counsel to report to this court the amount of refund until July 1, 1979; and this court having considered the final report concerning refund claims filed by counsel on July 2, 1979 and the subsequent joint motion of the parties for the entry of a stipulated order confirming amount and directing refund of state taxes, now therefore,

IT IS ORDERED That the State of Washington make refund of sales and use taxes, determined by this court in its order of November 3, 1977 to have been impermissibly collected, to the United States in the amount of $2,061,509.07, which amount except as hereinafter provided shall constitute full and complete satisfaction of the liability of the State of Washington arising out of this court's order of November 3, 1977 such that no further refund shall be made to any other person or business entity based upon said November 3, 1977 order of this court; and it is further,

ORDERED That the State of Washington shall pay interest on the aforesaid amount of refund at the rate provided in RCW 82.32.060, from such date of payment of the taxes ordered refunded as the parties have identified and agreed upon, through the date of refund; and it is further,

ORDERED That this refund including interest shall be paid in the form of a single warrant issued by the State of Washington payable to the Department of the Treasury of the United States of America; and it is further,

ORDERED That should the statutes of the State of Washington invalidated by this court in its order entered in this cause on November 3, 1977 be subsequently declared valid by the highest court to enter a final judgment thereon the United States shall forthwith, upon

demand by the State of Washington, repay to the State of Washington in the form of a single negotiable instrument all funds refunded to the United States pursuant to this order together with interest at the rate now provided in RCW 82.32.050 from the date of refund by the State of Washington of the amounts provided herein through the date of payment by the United States; and it is further,

ORDERED That with respect to those amounts of taxes which the parties agree still remain in dispute and which are referred to by the parties as taxes relating to "public road building projects", the parties shall promptly prepare for the lodging of a pre-trial order in accordance with the order of this Court entered September 24, 1980, in No. C78-596V. In the event the court shall subsequently determine at trial in No. C78-596V that other amounts of taxes remaining in issue between the parties in this cause are to be refunded, such amounts shall be paid by the State of Washington to the United States upon entry of further order of the court, such refund to be paid with interest computed in the same manner as elsewhere provided in this order. It is further

ORDERED That nothing contained in this order shall be construed to indicate agreement by the State of Washington that plaintiff United States of America is as a matter of law entitled to the refund ordered herein; and it is further

ORDERED That the order of November 3, 1977 as previously amended is hereby modified as provided herein.

DATED this 14th day of November, 1980.

/s/ Donald S. Voorhees
DONALD S. VOORHEES
UNITED STATES DISTRICT JUDGE

Presented by:

/s/ Leland T. Johnson
LELAND T. JOHNSON
Senior Assistant Attorney General
Of Attorneys for Defendants

Approved for Entry:

/s/ John T. McCarthy
Trial Attorney, Tax Division
U.S. Department of Justice

APPENDIX F

No. 78-1424

IN THE

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

UNITED STATES OF AMERICA,

Appellee,

VS.

STATE OF WASHINGTON; DEPARTMENT OF REVENUE OF THE STATE OF WASHINGTON; and CHARLES W. HODDE, Director of Revenue, and his successors in office,

Appellants.

NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES

KENNETH O. EIKENBERRY
Attorney General
State of Washington

LELAND T. JOHNSON
TIMOTHY R. MALONE
Assistant Attorneys General
Temple of Justice
Olympia, Washington 98504
(206) 753-5528

Notice is hereby given that the defendants above named hereby appeal to the Supreme Court of the United States from the judgment of the United States Court of Appeals for the Ninth Circuit entered August 24, 1981, affirming the judgment previously entered by the United

States District Court for the Western District of Washington holding that the sales and use tax statutes of the State of Washington unconstitutionally discriminate against those with whom the United States deals under the Supremacy Clause of the United States Constitution.

This appeal is taken pursuant to 28 U.S.C. §1254(2).

DATED this 13th day of November, 1981.

KENNETH O. EIKENBERRY
Attorney General
State of Washington

/s/ Leland T. Johnson
LELAND T. JOHNSON
Assistant Attorney General

/s/ Timothy R. Malone
TIMOTHY R. MALONE
Assistant Attorney General

Attorneys for Appellants.

PROOF OF SERVICE

I, LoRay Walker, a secretary in the Office of the Attorney General, State of Washington, depose and say: that on the 13th day of November, 1981 I served a copy of the foregoing Notice of Appeal to the Supreme Court of the United States on the appellee herein, by depositing copies thereof addressed to: Gene Anderson, United States Attorney, United States Courthouse, 1010 Fifth Avenue, Seattle, Washington 98104, to the Solicitor General, United States Department of Justice, Washington, D.C. 20530, and to John J. McCarthy, Chief, Special Litigation,

Tax Division, United States Department of Justice, Washington, D.C. 20530.

/s/ LoRay W. Walker
LoRay W. Walker

Subscribed and Sworn to before me this 13th day of November, 1981.

/s/ _____
Notary Public in and for the State of Washington, residing at Olympia.

AMENDED PROOF OF SERVICE

I, LoRay Walker, a secretary in the Office of the Attorney General, State of Washington, depose and say: that on the 13th day of November, 1981 I served a copy of the foregoing Notice of Appeal to the Supreme Court of the United States on the appellee herein, by depositing copies thereof addressed to: Gene Anderson, United States Attorney, United States Courthouse, 1010 Fifth Avenue, Seattle, Washington 98104, to the Solicitor General, United States Department of Justice, Washington, D.C. 20530, and to John J. McCarthy, Chief, Special Litigation, Tax Division, United States Department of Justice, Washington, D.C. 20530, with first-class postage prepaid in compliance with United States Supreme Court Rule No. 28. A copy of the foregoing amended proof of service has been

served this day on the aforesaid parties in the same manner.

All parties required to be served herein have been served.

/s/ LoRay W. Walker
LoRay W. Walker

Subscribed and Sworn to before me this 17th day of November, 1981.

/s/ Phyllis R. Weaver
Notary Public in and for the State of Washington, residing at Olympia.

APPENDIX G

ARTICLE VI

This Constitution, and the laws of the United States which shall be made in pursuance thereof; and all treaties made, or which shall be made, under the authority of the United States, shall be the supreme law of the land; and the judges in every state shall be bound thereby, any thing in the Constitution or laws of any state to the contrary notwithstanding.

APPENDIX H

RCW 82.04.050

"Sale at retail" or "retail sale" means every sale of tangible personal property (including articles produced, fabricated, or imprinted) to all persons irrespective of the nature of their business and including, among others, without limiting the scope hereof, persons who install, repair, clean, alter, improve, construct, or decorate real or personal property of or for consumers other than a sale to a person who (a) purchases for the purpose of resale as tangible personal property in the regular course of business without intervening use by such person, or (b) installs, repairs, cleans, alters, imprints, improves, constructs, or decorates real or personal property of or for consumers, if such tangible personal property becomes an ingredient or component of such real or personal property without intervening use by such person, or (c) purchases for the purpose of consuming the property purchased in producing for sale a new article of tangible personal property or substance, of which such property becomes an ingredient or component or is a chemical used in processing, when the primary purpose of such chemical is to create a chemical reaction directly through contact with an ingredient of a new article being produced for sale. The term shall include every sale of tangible personal property which is used or consumed or to be used or consumed in the performance of any activity classified as a "sale at retail" or "retail sale" even though such property is resold or utilized as provided in (2), (b), or (c) above following such use. The term also means every sale of tangible personal property to persons engaged in any business which is taxable under RCW 82.04.280, subsections (2) and (7) and RCW 82.04.290. * * * *

The term shall not include the sale of or charge made for labor and services rendered in respect to the constructing, repairing, decorating, or improving of new or existing buildings or other structures under, upon, or above real property of or for the United States, any instrumentality thereof, or a county or city housing au-

thority created pursuant to chapter 35.82 RCW, including the installing, or attaching of any article of tangible personal property therein or thereto, whether or not such personal property becomes a part of the realty by virtue of installation. Nor shall the term include the sale of services or charges made for the clearing of land and the moving of earth of or for the United States, any instrumentality thereof, or a county or city housing authority.

RCW 82.04.190

"Consumer" means the following:

(1) Any person who purchases, acquires, owns, holds, or uses any article of tangible personal property irrespective of the nature of his business and including, among others, without limiting the scope hereof, persons who install, repair, clean, alter, improve, construct, or decorate real or personal property of or for consumers other than for the purpose (a) of resale as tangible personal property in the regular course of business or (b) of incorporating such property as an ingredient or component of real or personal property when installing, repairing, cleaning, altering, imprinting, improving, constructing, or decorating such real or personal property of or for consumers or (c) of consuming such property in producing for sale a new article of tangible personal property or a new substance, of which such property becomes an ingredient or component or as a chemical used in processing, when the primary purpose of such chemical is to create a chemical reaction directly through contact with an ingredient of a new article being produced for sale;

(2) Any person engaged in any business activity taxable under RCW 82.04.290;

(3) Any person engaged in the business of contracting for the building, repairing or improving of any street, place, road, highway, easement, right of way, mass public transportation terminal or parking facility, bridge, tunnel, or trestle which is owned by a municipal corporation or political subdivision of the state of Washington or by the United States and which is used or to be used primarily fo foot or vehicular traffic including mass transportation ve-

hicles of any kind as defined in RCW 82.04.280, in respect to tangible personal property when such person incorporates such property as an ingredient or component of such publicly owned street, place, road, highway, easement, right of way, mass public transportation terminal or parking facility, bridge, tunnel, or trestle by installing, placing or spreading the property in or upon the right of way of such street, place, road, highway, easement, bridge, tunnel, or trestle or in or upon the site of such mass public transportation terminal or parking facility;

(4) Any person who is an owner, lessee or has the right of possession to or an easement in real property which is being constructed, repaired, decorated, improved, or otherwise altered by a person engaged in business excluding only (a) municipal corporations or political subdivisions of the state in respect to labor and services rendered to their real property which is used or held for public road purposes, and (b) the United States, instrumentalities thereof, and county and city housing authorities created pursuant to chapter 35.82 RCW in respect to labor and services rendered to their real property. Nothing contained in this or any other subsection of this definition shall be construed to modify any other definition of "consumer";

(5) Any person who is an owner, lessee, or has the right of possession to personal property which is being constructed, repaired, improved, cleaned, imprinted, or otherwise altered by a person engaged in business;

(6) Any person engaged in the business of constructing, repairing, decorating, or improving new or existing buildings or other structures under, upon, or above real property of or for the United States, any instrumentality thereof, or a county or city housing authority created pursuant to chapter 35.82 RCW, including the installing or attaching of any article of tangible personal property therein or thereto, whether or not such personal property becomes a part of the realty by virtue of installation. Any such person shall be a consumer within the meaning of this subsection in respect to tangible personal property incorporated into, installed in, or attached to such building or other structure by such person.

RCW 82.08.020

There is levied and there shall be collected a tax on each retail sale in this state equal to four and one-half percent of the selling price: * * * *

RCW 82.08.050

The tax hereby imposed shall be paid by the buyer to the seller, and each seller shall collect from the buyer the full amount of the tax payable in respect to each taxable sale in accordance with the schedule of collections adopted by the department pursuant to the provisions of RCW 82.08.060. The tax required by this chapter, to be collected by the seller, shall be deemed to be held in trust by the seller until paid to the department, and any seller who appropriates or converts the tax collected to his own use or to any use other than the payment of the tax to the extent that the money required to be collected is not available for payment on the due date as prescribed in this chapter shall be guilty of a gross misdemeanor.

In case any seller fails to collect the tax herein imposed or having collected the tax, fails to pay it to the department in the manner prescribed by this chapter, whether such failure is the result of his own acts or the result of acts or conditions beyond his control, he shall, nevertheless, be personally liable to the state for the amount of the tax.

The amount of tax, until paid by the buyer to the seller or to the department, shall constitute a debt from the buyer to the seller and any seller who fails or refuses to collect the tax as required with intent to violate the provisions of this chapter or to gain some advantage or benefit, either direct or indirect, and any buyer who refuses to pay any tax due under this chapter shall be guilty of a misdemeanor. The tax required by this chapter to be collected by the seller shall be stated separately from the selling price and for purposes of determining the tax due from the buyer to the seller and from the seller to the department it shall be conclusively presumed that the selling price quoted in any price list, sales document, contract

or other agreement between the parties does not include the tax imposed by this chapter.

Where a buyer has failed to pay to the seller the tax imposed by this chapter and the seller has not paid the amount of the tax to the department, the department may, in its discretion, proceed directly against the buyer for collection of the tax, in which case a penalty of ten percent may be added to the amount of the tax for failure of the buyer to pay the same to the seller, regardless of when the tax may be collected by the department; and all of the provisions of chapter 82.32 RCW, including those relative to interest and penalties, shall apply in addition; and, for the sole purpose of applying the various provisions of chapter 82.32 RCW, the fifteenth day of the month following the tax period in which the purchase was made shall be considered as the due date of the tax.

RCW 82.04.280

Upon every person * * * (7) engaging in activities which bring a person within the definition of consumer contained in RCW 82.04.190(6), as now or hereafter amended; as to such persons, the amount of tax on such business shall be equal to the gross income of the business multiplied by the rate of forty-four one hundredths of one percent.

RCW 82.12.010

For the purposes of this chapter:

(1) "Value of the article used" shall mean the consideration, whether money, credit, rights, or other property, expressed in terms of money, paid or given or contracted to be paid or given by the purchaser to the seller for the article of tangible personal property, the use of which is taxable under this chapter. The term includes, in addition to the consideration paid or given or contracted to be paid or given, the amount of any tariff or duty paid with respect to the importation of the article used. In case the article used is acquired by lease or by gift or is extracted, produced, or manufactured by the person

using the same or is sold under conditions wherein the purchase price does not represent the true value thereof, the value of the article used shall be determined as nearly as possible according to the retail selling price at place of use of similar products of like quality and character under such rules and regulations as the department of revenue may prescribe.

In case the articles used are acquired by bailment, the value of the use of the articles so used shall be in an amount representing a reasonable rental for the use of the articles so bailed, determined as nearly as possible according to the value of such use at the places of use of similar products of like quality and character under such rules and regulations as the department of revenue may prescribe: PROVIDED, That in case any such articles of tangible personal property are used in respect to the construction, repairing, decorating, or improving of, and which become or are to become an ingredient or component of, new or existing buildings or other structures under, upon, or above real property of or for the United States, any instrumentality thereof, or a county or city housing authority created pursuant to chapter 35.82 RCW, including the installing or attaching of any such articles therein or thereto, whether or not such personal property becomes a part of the realty by virtue of installation, then the value of the use of such articles so used shall be determined according to the retail selling price of such articles, or in the absence of such a selling price, as nearly as possible according to the retail selling price at place of use of similar products of like quality and character or, in the absence of either of these selling price measures, such value may be determined upon a cost basis, in any event under such rules and regulations as the department of revenue may prescribe.

In the case of articles manufactured or produced by the user and used in the manufacture or production of products sold or to be sold to the department of defense of the United States, the value of the articles used shall be determined according to the value of the ingredients of such articles.

(2) "Use," "used," or "put to use" shall have their ordinary meaning, and shall mean the first act within this state by which the taxpayer takes or assumes dominion or control over the article of tangible personal property (as a consumer), and include installation, storage, withdrawal from storage, or any other act preparatory to subsequent actual use or consumption within this state;

(3) "Taxpayer" and "purchaser" include all persons included within the meaning of the word "buyer" and the word "consumer" as defined in chapters 82.04 and 82.08 RCW;

(4) "Retailer" means every person engaged in the business of selling tangible personal property at retail and every person required to collect from purchasers the tax imposed under this chapter;

(5) The meaning ascribed to words and phrases in chapters 82.04 and 82.08 RCW, insofar as applicable, shall have full force and effect with respect to taxes imposed under the provisions of this chapter. "Consumer," in addition to the meaning ascribed to it in chapters 82.04 and 82.08 RCW insofar as applicable, shall also mean any person who distributes or displays, or causes to be distributed or displayed, any article of tangible personal property, except newspapers, the primary purpose of which is to promote the sale of products or services.

Presently uncodified section 3 of Chapter 1, Laws of 1975-76, 2nd ex. sess. amending section 4 of chapter 90, Laws of 1975, 1st ex. sess.

In the event any person has entered into a contract prior to July 1, 1975 or has bid upon a contract prior to July 1, 1975 and has been awarded the contract after July 1, 1975, the additional taxes imposed by chapter 90, Laws of 1975 1st ex. sess., section 5, chapter 291, Laws of 1975 1st ex. sess. and this 1975 amendatory act shall not be required to be paid by such person in carrying on activities in the fulfillment of such contract.

RCW 82.12.020

There is hereby levied and there shall be collected from every person in this state a tax or excise for the

privilege of using within this state as a consumer any article of tangible personal property purchased at retail, or acquired by lease, gift, repossession, or bailment, or extracted or produced or manufactured by the person so using the same, or otherwise furnished to a person engaged in any business taxable under RCW 82.04.280, subsections (2) or (7). This tax will not apply with respect to the use of any article of tangible personal property purchased, extracted, produced or manufactured outside this state until the transportation of such article has finally ended or until such article has become commingled with the general mass of property in this state. This tax shall apply to the use of every article of tangible personal property, including property acquired at a casual or isolated sale, and including byproducts used by the manufacturer thereof, except as hereinafter provided, irrespective of whether the article or similar articles are manufactured or are available for purchase within this state. Except as provided in subdivision (2) of RCW 82.12.030, payment by one purchaser or use of tangible personal property of the tax imposed by chapter 82.08 or 82.12 RCW shall not have the effect of exempting any other purchaser or user of the same property from the taxes imposed by such chapters. The tax shall be levied and collected in an amount equal to the value of the article used by the taxpayer multiplied by the rate of four and one-half percent.

Joint Appendix

Office - Supreme Court, U.S.
FILED
JUN 24 1982
ALEXANDER L. STEVAS,
CLERK

No. 81-969

IN THE

SUPREME COURT

OF THE

UNITED STATES

OCTOBER TERM, 1981

STATE OF WASHINGTON, et al.,

Appellants,

v.

UNITED STATES OF AMERICA,

Appellee.

ON APPEAL FROM THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

JOINT APPENDIX

KENNETH O. EIKENBERRY,
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Counsel for Appellees

APPEAL DOCKETED NOVEMBER 20, 1981
PROBABLE JURISDICTION NOTED MAY 17, 1982

STATE PRINTING PLANT OLYMPIA, WASHINGTON

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NOTATION

The following decision, judgment, orders and notice have been omitted in printing this joint appendix because they appear on the following pages in the appendix to the printed Jurisdictional Statement:

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Notice of Appeal to the Supreme Court of the United States F-1

RELEVANT DOCKET ENTRIES

THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF WASHINGTON

DATE	NR	PROCEEDINGS
1977		
May 12	1	Filed c.c. of Stipulation and Order allowing dismissal (of C76-105V) and refiling.
May 12	1a	Filed complaint and issued summons.
May 12	5	Filed Answer.
May 12	7	Filed Pltf's motion for partial summary judgment.
May 12	8	Filed Pltf's points/auth. in support of motion for partial summ. judgm.
May 12	9	Filed affidavit of William Frake.
May 12	10	Filed affidavit of Captain Ernest R. Stacey.
May 12	11	Filed affidavit of James F. Walsh w/ exhibits attached.
May 12	12	Filed Deft's motion for summary judgment of dismissal.
May 12	13	Filed Deft's memorandum in opposition to Pltf's motion for partial summary judgment and in support of defts' motion for summary judgment of dismissal.
May 12	16	Filed Pltf's reply points and authorities in further support of its motion for partial summary judgment and in opposition to Defts' motion for summary judgment of dismissal.

May 12	17	Filed second affidavit of James F. Walsh. Per STIPULATION Pltf's Motion for Partial Summary Judgment- and- Deft's Motion for Summary Judgment DISMISSAL, ARE NOTED FOR JUNE 10, 1977.
June 1	18	Filed Deft's reply memorandum in opposition to Pltff's motion for Partial Summary Judgment and in support of Deft's Motion for Summary Judgment of Dismissal.
Oct 7		Ent. hearing of Oral Argument on Summary Jdmt motions, after argument of counsel Court takes the motions under submission.
Nov 3	21	Filed and entered Order on Cross-motions for Summary Jdmt. as follows: defts are enjoined from assessing or collecting Sales or Use Tax from pltff, and that defts repay the sale and use taxes which have been impermissibly collected. Counsel for pltff and defts are directed to meet to determine the amount of taxes to be refunded. Counsel shall report back to the Court within 60 days of this Order. If parties are unable to agree as to the amt of taxes to be refunded this Court will at that time consider the apptment of a special master to make that determination. Copy to Counsel.
Dec 30	22	Filed joint motion of Pltff U.S.A. and of deft Wash. State for amendment to Courts Order on Cross-motion for Summary Judgment.
Dec 30	23	Filed and entered Order on agreed motion amending & supplementing order of Nov. 3, 1977, issue of amt of taxes to be refunded severed for separate Trial; Govt. to advise State by Mar 3, 1978 which taxes

		it claims should be refunded and State to report back by July 1, 1978 & injunction modified.
Dec 30	24	Filed Defts notice of Appeal. Copy to C of A.
	25	Filed Cost Bond on Appeal $250.00 National Surety Corp.
1978		
Jan 20	26	Filed defts designation of Record on Appeal, copy to C of A.
Jan 27		Ent pltfs designation of record on appeal, per phone call requesting the entire record.
Feb 1	27	Filed pltffs designation of record on appeal.
Feb 6		Mailed Record on Appeal to C of A.
Mar 13		Filed receipt from C of A of Record on Appeal, assigned number 78-1424.
1980		
Nov 17	35	ORDER — confirming amt. & directing refund of State Taxes. C to c.
1981		
Sep 17	36	JUDGMENT — C of A Affirming District Court. C to c.

THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

DATE	FILINGS — PROCEEDINGS
1978	
FEB 27	DOCKETED CAUSE AND ENTERED APPEARANCES OF COUNSEL.

MAR 16	FILED AS OF 2/27/78, CERT TRANS OF RECORD ON APPEAL IN TWO VOLS., VOL I, PLDGS, THREE CERT CYS., VOL II, R/T'S, ORIG & ONE CY.
1980	
May 7	ARGUED & SUBMITTED BEFORE: ANDERSON, SKOPIL, CJJ, WILLIAM M. BYRNE, DJ FROM (CENTRAL, CA.)
1981	
Aug 24	ORDERED OPINION (Byrne) FILED & JUDG TO BE FILED & ENTD.
Aug 24	Filed Opinion —Affirmed.
Aug 24	Filed & Entered Judgment.
15 SEP	MANDATE ISSUED
Nov 19	Filed, as of Nov 16, 1981, appellants' NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES with amended proof of service dated 11/17/81, re CA judgment, pursuant to 28 U.S.C. §1254(2).
Nov 30	Recvd SC notice of filing petition for cert on 11/20/81, SC#81-969.
1982	
May 20	Filed certified copy of SC order of 5/17/82, noting probable jurisdiction. (copies to panel)

IN THE UNITED STATES DISTRICT COURT FOR THE
WESTERN DISTRICT OF WASHINGTON

CIVIL ACTION NO. C77-355V

COMPLAINT FOR DECLARATORY JUDGMENT, INJUNCTIVE RELIEF, AND REFUND OF TAXES

[Filed May 12, 1977]

UNITED STATES OF AMERICA,

Plaintiff,

v.

STATE OF WASHINGTON; DEPARTMENT OF REVENUE OF THE STATE OF WASHINGTON; and MARY ELLEN McCAFFREE, Director of Revenue, and her successors in office,

Defendants.

Comes now the plaintiff, United States of America. by its attorney, Stan Pitkin, United States Attorney for the Western District of Washington, and complaining of the defendants alleges as follows:

1. This is a civil action brought by the United States for delcaratory judgment, injunctive relief, and refund of State of Washington State and local sales and use taxes collected by the defendants from July 1, 1975, to the present.

2. This action is brought by the United States under the direction of the Attorney General of the United States to protect the pecuniary interest and sovereign rights of the United States.

3. Jurisdiction over this action is conferred upon this Court by Title 28, United States Code, Sections 1345 and 2201 since the action is commenced by the United States.

4. An actual controversy, as is more fully described below, has arisen and now exists between the United States and the defendants concerning their respective rights and obligations.

5. Plaintiff United States is a corporate sovereign and body politic.

6. Defendant State of Washington is one of the States forming the Union of the United States of America, and is joined as a defendant herein as this action involves the application of the Washington Sales and Use Tax Act, Chapter 82.08, 82.12, and 82.14, Revised Code of Washington, as amended, (hereinafter referred to as the "Act"), to construction activity by the United States within the State of Washington.

7. Defendant Department of Revenue is the department of the State of Washington charged with the enforcement of the Act and the assessment and collection of State of Washington State and local sales and use taxes.

8. Defendant Mary Ellen McCaffree, Director of Revenue of the State of Washington, is the State of Washington official charged with the enforcement of the Act and who has illegally and erroneously assessed and collected from the plaintiff's contractors, subcontractors or suppliers Washington State and local sales and use taxes on behalf of the State of Washington and its political subdivisions pursuant to the alleged authority to do so under the Act with respect to such construction activity by the United States and is named as defendant herein in her official capacity.

9. In the operations of the various Departments and agencies of the United States, there has been, there is now, and there will be, a considerable amount of construction activity or improvements to real property undertaken by the United States within the State of Washington.

10. The United States has and will continue to enter into contracts with private construction contractors in order to effect this construction.

11. At all times here relevant, defendants, by rulings, regulations or otherwise, have construed and enforced the Act, as amended effective July 1, 1975, as requiring payment of Washington State and local sales and use taxes with respect to such construction under such contracts, and the defendants have refused to change their position

and continue to enforce or threaten to enforce the Act and continue to collect or threaten to collect such taxes with respect to such construction.

12. Payments by such contractors, subcontractors or suppliers of Washington State and local sales and use taxes claimed by the defendants to be due under the Act with respect to such construction have or will, it is believed, since July 1, 1975, exceed $1,000,000.

13. Provisions of such contracts required, and in accordance therewith the United States has made, or has agreed to make, payment to said contractors for the amounts of taxes paid.

14. The United States is entitled to the benefit of any recovery of any part of said payments received by the defendants.

15. The defendants' said rulings, regulations, construction and enforcement of the Act are and have been erroneous, unlawful, and without legal force or effect and said taxes have been erroneously and illegally demanded, collected and received by defendants because:

(a) With respect to such construction by the United States, the legal incidence of the sales and use taxes imposed by the Act falls on the United States and, therefore, the sales and use taxes infringe the United States' immunity, under the Federal Constitution, from state and local taxation; and

(b) With respect to construction by the United States, the sales and use taxes imposed by the Act discriminate against the United States and its contractors in violation of the Federal Constitution because the sales and use taxes are imposed with respect to construction by the United States in a manner unlike that with respect to other construction in the State of Washington.

WHEREFORE, plaintiff prays judgment:

1. Declaring that

(a) With respect to such construction by the

United States, the legal incidence of the sales and use taxes imposed by the Act falls on the United States, and, therefore, the sales and use taxes infringe the United States' immunity, under the Federal Constitution, from state and local taxation; and

(b) With respect to construction by the United States, the sales and use taxes imposed by the Act discriminate against the United States and its contractors in violation of the Federal Constitution because the sales and use taxes are imposed with respect to construction by the United States in a manner unlike that with respect to other construction in the State of Washington.

2. Enjoining the defendants during the pendency of this action and permanently thereafter from imposing, assessing or collecting the Washington State and local sales and use tax with respect to said construction;

3. Adjudging that the tax payments demanded, remitted to, and received by the defendants with respect to the construction by the United States were erroneously remitted and illegally demanded and received;

4. Directing refund to the United States of all said payments with appropriate interest; and

5. Granting the United States such other and further relief as may be just and proper.

DATED: February 11, 1976.

JOHN J. MCCARTHY
Chief, General Litigation Sec.

WILLIAM H. FRAKE
Trial Attorney
General Litigation Section, Tax Division
Department of Justice
Washington, D.C. 20530
202-739-2733

STAN PITKIN
United States Attorney

/s/ _____
CHARLES F. MANSFIELD
Assistant United States Attorney

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF
WASHINGTON

CIVIL ACTION

NO. C77-355V

ANSWER

[Filed May 12, 1977]

UNITED STATES OF AMERICA,

Plaintiff,

vs.

STATE OF WASHINGTON; DEPARTMENT OF REVENUE OF THE STATE OF WASHINGTON; and MARY ELLEN McCAFFREE, Director of the Department of Revenue, and her successors in office,

Defendants.

COME Now the defendants, State of Washington, Department of Revenue of the State of Washington, and Mary Ellen McCaffree, Director of the Department of Revenue, et al. (hereinafter called "defendants"), by their attorneys Slade Gorton, Attorney General, State of Washington and by Richard H. Holmquist and John R. Wasberg, Assistant Attorneys General, and answer the Complaint of the plaintiff in the above-styled cause as follows:

1. In answer to paragraph 1 of said Complaint, the defendants admit that this is a civil action brought by the United States for declaratory judgment and injunctive relief and refund of certain Washington State state and local sales and use taxes allegedly collected by defendants from July 1, 1975, to the present, but defendants specifically deny all other allegations contained therein.

2. In answer to paragraph 2 of said Complaint, defendants admit that the pecuniary interests of plaintiff may be indirectly affected by the Washington State

legislation under challenge in the above-styled cause, but specifically deny that the sovereign rights of the United States are adversely affected by the Washington state legislation under challenge in the above-styled cause; further, defendants state that they lack sufficient knowledge or information to admit or deny both the allegation regarding the motivation of the plaintiff in maintaining the above-styled cause and the allegation that said cause is brought under the direction of the Attorney General of the United States and, accordingly, defendants deny said allegations.

3. In answer to paragraph 3 of said Complaint, defendants admit jurisdiction over the above-styled cause is conferred upon the Court by 28 U.S.C. §§1345 and 2201, subject to other applicable provisions of law; except as expressly admitted herein, defendants specifically deny the allegations contained in said paragraph 3 of the Complaint.

4. In answer to paragraphs 4 and 5 of said Complaint, defendants admit the allegations contained therein.

5. In answer to paragraph 6 of said Complaint, defendants admit that defendant State of Washington is one of the states forming the Union of the United States of America; defendants further admit that the above-styled cause involves the application of three statutes of the State of Washington, namely, [1] chapter 90, Washington Laws of 1975, 1st extraordinary session, [2] chapter 291, Washington Laws of 1975, 1st extraordinary session (more particularly, section 5 thereof), and [3] chapter 1, Washington Laws of 1975, 2nd extraordinary session, duly certified copies of which are attached hereto, and by this reference incorporated herein, as, respectively, Exhibits 1, 2, and 3 to this Answer. Except as expressly admitted herein, defendants specifically deny the allegations contained in said paragraph 6 of the Complaint.

6. In answer to paragraph 7 of said Complaint, defendants admit that the defendant Department of Revenue of the State of Washington is the department of the State of Washington charged with assessment and

collection of all State of Washington state and local sales and use taxes and enforcement of all State of Washington sales and use tax statutes.

7. In answer to paragraph 8 of said Complaint, defendants admit that defendant Mary Ellen McCaffree named as a defendant in her official capacity is the duly appointed, qualified, and acting Director of Revenue of the State of Washington, and that in her capacity as said Director, defendant McCaffree is the chief executive officer of defendant Department of Revenue of the State of Washington and, as such, is the state official charged, *inter alia,* with the duty to assess and collect all taxes and administer all programs relating to taxes which are the reponsibility of the defendant Department of Revenue under the laws of the State of Washington; defendants state that they presently lack sufficient knowledge or information to admit or deny the allegation that any of the defendants have assessed or collected from plaintiff's contractors, subcontractors or suppliers State of Washington state and local sales and use taxes pursuant to the three Washington statutes attached hereto as Exhibits 1 through 3 and, accordingly, defendants deny said allegation. Except as denied for lack of knowledge or information or admitted herein, defendants specifically deny all other allegations contained in said paragraph 8 of the Complaint.

8. In answer to paragraph 9 of said Complaint, defendants state that they lack sufficient knowledge or information to admit or deny the allegations contained therein and, accordingly, defendants deny all the allegations contained in said paragraph 8 of the Complaint.

9. In answer to paragraph 10 of said Complaint, defendants admit that plaintiff has entered and will continue to enter into contracts with private construction contractors in order to effect constructions projects on federal property within the State of Washington for the benefit and use of plaintiff; except as expressly admitted herein, defendants specifically deny the allegations contained in said paragraph 10 of the Complaint.

10. In answer to paragraph 11 of said Complaint, defendants admit that they have construed and will continue to construe the laws of the State of Washington in general and in particular the three Washington statutes attached hereto as Exhibits 1 through 3 as requiring payment by private contractors of certain Washington State state and local sales and use taxes with respect to portions of the construction activities described in paragraph 9 of this Answer. Defendants further admit that they will, in the ordinary course of performing their duties to assess and collect Washington State taxes which are their responsibility under Washington law, take such enforcement actions as are provided by law in order to collect such taxes with respect to such construction activities. Except as expressly admitted herein, defendants specifically deny the allegations contained in said paragraph 11 of the Complaint.

11. In answer to paragraphs 12, 13, and 14 of said Complaint, defendants state that they lack sufficient knowledge or information to admit or deny the allegations contained therein and, accordingly, defendants deny said allegations.

12. In answer to paragraph 15 of said Complaint, defendants specifically deny the allegations contained therein.

AFFIRMATIVE DEFENSE

In further answer to the Complaint herein, and by way of affirmative defense, defendants allege that the State of Washington tax statutes at issue in the above-styled cause and attached hereto as Exhibits 1 through 3 to this Answer as well as the actions of defendants taken in furtherance of such statutes are in all respects consonant with the Constitution and laws of the United States.

WHEREFORE, having fully answered the Complaint of the plaintiff, defendants pray that the Complaint be dismissed with prejudice and that defendants be awarded their costs herein incurred and such other and further relief as may by this Court be deemed just and proper.

DATED this 14th day of May, 1976.

SLADE GORTON, Attorney General
State of Washington

By: /s/ _____
Richard H. Holmquist
Assistant Attorney General

/s/ _____
John R. Wasberg
Assistant Attorney General

STATE OF WASHINGTON)
) ss.
County of Thurston)

MARY ELLEN McCAFFREE, being first duly sworn, on oath deposes and says:

That she is one of the defendants above named in her capacity as Director of Revenue of the State of Washington and that she has read the within and foregoing Answer, knows the contents thereof, and believes the same to be true.

/s/ _____
MARY ELLEN McCAFFREE

SUBSCRIBED AND SWORN TO before me this 14th day of May, 1976.

[SEAL] /s/ _____
NOTARY PUBLIC in and for the State of Washington residing at Olympia.

IN THE UNITED STATES DISTRICT COURT FOR THE
WESTERN DISTRICT OF WASHINGTON

CIVIL ACTION NO. C77-355V

MOTION FOR PARTIAL SUMMARY JUDGMENT

UNITED STATES OF AMERICA,

Plaintiff,

v.

STATE OF WASHINGTON, et al.,

Defendants.

Comes now the plaintiff, United States of America, by its attorney Stan Pitkin, United States Attorney for the Western District of Washington, and respectfully moves this Court, pursuant to the provisions of Rule 56 of the Federal Rules of Civil Procedure, for an entry of partial summary judgment from this Court:

(1) Declaring that

(a) With respect to construction activity or improvements to real property undertaken by the United States within the State of Washington, the sales and use taxes imposed by Chapters 82.08, 82.12 and 82.14, Revised Code of Washington, as amended, and the rules and regulations promulgated thereunder, discriminate against the United States and its contractors in violation of the Supremacy Clause of the Federal Constitution in that the sales and use taxes are imposed upon contractors for the Federal Government as "consumers," but are not so imposed upon other construction contractors (including contractors for the state of Washington);

(b) With respect to construction activity or improvements to real property undertaken by the United States within the State of Washington in which tangible personal property is furnished by the United States to its

contractors for installation or incorporation into the property, the use tax imposed by Chapters 82.12 and 82.14, Revised Code of Washington, as amended, and the rules and regulations promulgated thereunder, discriminates against the United States and its contractors in violation of the Supremacy Clause of the Federal Constitution in that the use tax is imposed with respect to such property furnished by the United States to its contractors but the use tax is not imposed when property is furnished by others (including the State of Washington) to their contractors for installation or incorporation into the property;

(c) With respect to construction activity or improvements to real property undertaken by the United States within the State of Washington in which tangible personal property is furnished by the United States to its contractors for use in respect to such construction, improvement, installation, or incorporation, the use tax imposed by Chapters 82.12 and 82.14, Revised Code of Washington, as amended, and the rules and regulations promulgated thereunder, discriminates against the United States and its contractors in violation of the Supremacy Clause of the Federal Constitution in that the use tax is imposed with respect to such property furnished by the United States to its contractors upon the basis of the retail selling price of the property but when property is acquired by bailment by others (including property bailed by the State of Washington), the use tax is upon the basis of the rental value of the property bailed; and

(d) With respect to construction activity or improvements to real property undertaken by the United States within the State of Washington, the legal incidence of the sales and use taxes imposed by Chapters 82.08, 82.12 and 82.14, Revised Code of Washington, as amended, and the rules and regulations promulgated thereunder, falls on the United States, and, therefore, the sales and use taxes infringe the United States immunity, under the Supremacy Clause of the Federal Constitution, from state and local taxation.

(2) Enjoining the defendants from imposing, assessing or collecting the taxes imposed by Chapters 82.08, 82.12 and 82.14, as amended, with respect to such construction, improvement, installation or incorporation by the United States and its contractors;

(3) Adjudging that the United States is entitled to recover, and directing a refund, with interest, of all taxes collected by the State of Washington under Chapters 82.08, 82.12 and 82.14, as amended, with respect to such construction, improvement, installation or incorporation, by the United States and its contractors for which the United States pursuant to its contractual obligation with its contractors has reimbursed its contractors and is entitled to the benefit of such recovery; and

(4) Directing a hearing, before the Court or a referee, for the purpose of fixing the amount to which the United States is entitled, if the parties are unable to agree; on the grounds that the facts on which the United states relies, as to which there is no genuine triable issue, establish that, as a matter of law, (a) the United States is entitled to the relief sought on this motion and (b) the defendant does not have any valid defense to any of the relief sought.

The motion will be made upon this document, the complaint herein, the affidavits and exhibits of plaintiff, the Points and Authorities filed in support of this motion, and all other papers filed and proceedings had herein by the time the motion is heard.

Plaintiff requests oral argument on this motion.

DATED: September 16, 1976.

STAN PITKIN
United States Attorney

/s/ _____
CHARLES F. MANSFIELD
Assistant United States Attorney

OF COUNSEL:

JOHN J. MCCARTHY, Chief
Civil Trial Section, Central Region

/s/ _____
WILLIAM H. FRAKE
Trial Attorney
Civil Trial Section, Central Region
Tax Division
U.S. Department of Justice
Washington, D.C. 20530

IN THE UNITED STATES DISTRICT COURT FOR THE
WESTERN DISTRICT OF WASHINGTON

CIVIL ACTION NO. C77-355V

AFFIDAVIT OF WILLIAM H. FRAKE

UNITED STATES OF AMERICA,

Plaintiff,

v.

STATE OF WASHINGTON, et al.,

Defendants.

CITY OF WASHINGTON)
) ss:
DISTRICT OF COLUMBIA)

WILLIAM H. FRAKE, being of lawful age and duly sworn, deposes and says:

1. That I am an attorney in the Tax Division, United States Department of Justice, Washington, D.C., and in such capacity am one of the attorneys representing the plaintiff United States in this action.

2. That in my capacity as trial attorney, I have reviewed my files in this case and have requested information from the various Government departments involved relating to the present controversy. Based upon a review of the files, and the information provided to me by the various departments, the following facts are, to the best of my knowledge, true and correct:

(a) This action is brought by the United States under the direction of the Attorney General of the United States at the request of several Government departments having construction within the State of Washington.

(b) Based upon my inquiry of those Government departments likely to engage in construction within the State of Washington, it is the usual practice to utilize "lump-sum fixed price" contracts containing standard United States General Services Administration (GSA) provisions (Standard Forms 19-A and 23-A) similar to plaintiff's Exhibits 1 and 2. In addition, such contracts for the most part contain a provision similar to Clause 103 of Exhibit 1 and Clause 74 of Exhibit 2 which require Washington sales and use taxes to be excluded from the contract price and billed separately to the Government and that any refund of such tax will inure to the benefit of the Government.

/s/ _____
WILLIAM H. FRAKE

Subscribed and sworn to before me
this 25th day of June, 1976.

/s/ _____
Notary Public

My Commission expires January 1, 1981.

IN THE UNITED STATES DISTRICT COURT FOR THE
WESTERN DISTRICT OF WASHINGTON

CIVIL ACTION NO. C77-355V

AFFIDAVIT OF CAPTAIN ERNEST R. STACEY

UNITED STATES OF AMERICA,

Plaintiff,

v.

STATE OF WASHINGTON, et al.,

Defendants.

COUNTY OF ARLINGTON)
) ss:
STATE OF VIRGINIA)

ERNEST R. STACEY, being of lawful age and duly sworn, deposes and says:

That I am a commissioned office of the United States Navy with the grade of Captain, Civil Engineer Corps, on active duty and presently assignd to serve as Officer in Charge of Construction, TRIDENT. I have served in this capacity since the fall of 1972. Based upon my personal knowledge of the facts of this case, the following facts are, to the best of my knowledge and belief, true:

(1) The TRIDENT System is a strategic nuclear deterrent force involving submarines, a missile system, and shore-based support facilities. My assignment is the overall responsibility for the planning, budgeting, design and construction of these shore-based support facilities.

(2) The facilities for the TRIDENT Support Site are being constructed at the Bangor Annex of the U.S. Naval Torpedo Station, Keyport, Washington. Construction began in October, 1974, and completion of facilities is programmed to provide for an initial operational capability of the TRIDENT Support Site by mid-1979.

When completed, it is estimated that $650,000,000 in construction contracts will have been expended.

(3) Construction of the TRIDENT Support Site is being accomplished by a number of prime contractors. The contracts between the United States and these contractors have been and are being awarded according to fiscal year phases. Attached hereto as plaintiff's Exhibit (1) is a true copy of the general provisions of one of these contracts, Contract N68248-74-C-5016 (hereafter referred to as Contract 5016) awarded to Huber, Hunt & Nichols, Inc. (hereafter referred to as HH&N) for the construction of the Missile Assembly Facilities (1975 Increment) at the TRIDENT Support Site in the amount of $10,930,000. The provisions of Exhibit (1) are representative of all construction contracts awarded by the United States Navy for the TRIDENT program in the State of Washington during the period involved in this litigation.

(4) Contract 5016 calls for the construction of six buildings and the installation and testing of certain Government-furnished property. Pursuant to the terms of this contract, HH&N will procure substantial quantities of construction and building materials and building system equipment (electrical, heating, cooling, etc.) for incorporation into the buildings.

(5) Government-furnished property may have been procured by the Government either within or without the State of Washington.

(6) As the construction of facilities at the TRIDENT Support Site nears completion, additional Government-furnished property, some of which will be of sophisticated design and high dollar-value, will be installed and tested by Government contractors. This installation and test will occur after the building structure is complete and all basic support systems for the building (light, heat, water, electricity, etc.) are complete. Frequently, as in the case of the Missile Assembly Facilities, where the value of installed equipment is estimated to be $19,400,000, the value of such Government-furnished property so far exceeds the cost of labor to install and test it, that the tax

sought to be collected approximates the value of the contract itself.

(7) As noted above in paragraph (3), Exhibit (1) is representative of all TRIDENT construction contracts. Exhibit (1) is a "lump-sum fixed-price" contract utilizing basic standard United States General Services Administration (GSA) provisions (Standard Forms 19-A and 23-A). Other provisions include those required by the Armed Services Procurement Regulations (ASPR). Exhibit (1) in Clause 103 includes a provision which requires Washington sales and use taxes to be excluded from the contract price and billed separately to the Government. Clause 103 further provides that any refund of such tax will inure to the benefit of the Government. Most contracts entered into prior to the effective date of the amendments to the Washington Sales and Use Tax Act which do not contain Clause 103 have been or will be modified to include substantially the same language as Clause 103 which will be applicable to all adjustments in contract price which may be later negotiated by the contract parties.

/s/ _____
CAPTAIN ERNEST R. STACEY

Subscribed and sworn to before me
this 21st day of June, 1976.

/s/ _____
Notary Public

My commission expires February 5, 1980.

[Exhibit No. 1 to Affidavit of Ernest R. Stacey]

C77-355V

NAV.FAC 4280/1 (7-66)
Supersedes NAVDOCKS 1337
S/N 0104-814-0000

CONTRACT N68248 74-C-5016
MISSILE ASSEMBLY FACILITIES
FY 1975 INCREMENT
TRIDENT SUPPORT SITE
NAVAL TORPEDO STATION, BANGOR ANNEX
KEYPORT, WASHINGTON

SEAL
[Department of the Navy
Facilities Engineering Command]

NAVAL FACILITIES ENGINEERING COMMAND
DEPARTMENT OF THE NAVY
WASHINGTON, D.C.

CONFORMED COPY

STANDARD FORM 73
JANUARY 1961 EDITION
GENERAL SERVICES ADMINISTRATION
FED PROC REG (41 CFR) 1-16 401

CONSTRUCTION CONTRACT

(See instructions on reverse)

CONTRACT NO.
N68248-74-C-5016

DATE OF CONTRACT
75 DEC 31

NAME AND ADDRESS OF CONTRACTOR
HUBER, HUNT & NICHOLS, INC.
P.O. Box 608
Santa Clara, CA 95052

CHECK APPROPRIATE BOX
- ☐ Individual
- ☐ Partnership
- ☐ Joint Venture
- ☒ Corporation, incorporated in the State of Indiana

DEPARTMENT OR AGENCY
Department of the Navy
Naval Facilities Engineering Command, OICC TRIDENT

CONTRACT FOR (*Work to be performed*)
MISSILE ASSEMBLY FACILITIES, FY 1975 INCREMENT

PLACE
TRIDENT Support Site, Naval Torpedo Station,
Bangor Annex, Keyport, Washington

CONTRACT PRICE (*Express in words and figures*)
TEN MILLION NINE HUNDRED THIRTY THOUSAND AND NO/100 DOLLARS
($10,930,000)

ADMINISTRATIVE DATA (*Optional*)

*See Reverse

SUBMIT INVOICES TO:	Resident Officer in Charge of Construction, Strategic Weapons, P.O. Box UU, Wycoff Station, Bremerton, Washington 98310
PAYMENT WILL BE MADE BY:	Commanding Officer, Navy Regional Finance Center Treasure Island, San Francisco, CA 94130

The United States of America (hereinafter called the Government), represented by the Contracting Officer executing this contract, and the individual, partnership, joint venture, or corporation named above (hereinafter called the Contractor), mutually agree to perform this contract in strict accordance with the General Provisions, Labor Standards Provisions, and the following designated specifications, schedules, drawings, and conditions:

Bid Items 1 and option Item 2 of NAVFAC Specification No. 68-74-5016 with Amendments Nos. 0001, 0002, 0003, and 0004.

The Contractor shall furnish a Performance Bond in the sum of $10,930,000.00 and a Payment Bond in the sum of $2,500,000.00.

This contract is rated DX-C2. Certified for National Defense use under DMS Regulation 1 and DPS Regulation 1.

WORK SHALL BE STARTED	WORK SHALL BE COMPLETED
On or before 76JAN15	**(See completion dates on reverse)

CONFORMED COPY

parties hereto:

*APPROPRIATION DATA: AA17X1205.2551 032 682680 00248 2A 000000 N35032106C75: $2,535,654.00 (O/A #76-373 and O/A #76-428)
AB17X1205.2551 032 682680 068248 2A 000000 N35032127C75: $1,807,755.00 (O/A #76-373 and O/A 76-428)
AC17X1205.2551 032 682680 068248 2A 000000 N35032101C75: $3,537,923.00 (O/A #76-374 and O/A #76-427)
AD17X1205.2551 032 682680 068248 2A 000000 N35032102C75: $486,931.00 (O/A #76-374 and O/A #76-427)
AE17X1205.2551 032 682680 068248 2A 000000 N35032104C75: $2,421,737.00 (O/A #76-374 and O/A #76-427)
AF17X1205.2561 032 682680 068248 2A 000000 N35032208C76: $140,000.00 (O/A #76-386)

**Completion dates in accordance with paragraph 1A.4 of NAVFAC Specification 68-74-5016:

Phase IA ..... 30 March 1976
Phase IIA ..... 1 October 1976
Phase IIIA ..... 1 October 1976
Phase IVA ..... 30 November 1976
Phase VA ..... 30 December 1976
Phase VIA ..... 29 January 1977
Phase VIIA ..... 28 February 1977
Phase VIIIA ..... 30 March 1977
Phase IXA ..... 1 October 1976
Phase XA ..... 29 April 1977
Phase XIA ..... 9 April 1977
Phase IB ..... 30 March 1977

In witness whereof, the parties hereto have executed this contract as of the date entered on the first page hereof.

THE UNITED STATES OF AMERICA	CONTRACTOR
By /s/ Cecelia M. Lane	HUBER, HUNT & NICHOLS, INC.
CECELIA M. LANE	*(Name of Contractor)*
Director, Contracts Division,	By /s/ W. B. Huffman
OICC TRIDENT, For Commander,	*(Signature)*
Naval Facilities Engineering Command	President
Contracting Officer	*(Title)*
(Official Title)	

INSTRUCTIONS

1. The full name and business address of the Contractor must be inserted in the space provided on the face of the form. The Contractor shall sign in the space provided above with his usual signature and typewrite or print his name under the signature.

2. An officer of a corporation, a member of a partnership, or an agent signing for the Contractor shall place his signature and title after the word "By" under the name of the Contractor. A contract executed by an attorney or agent on behalf of the Contractor shall be accompanied by two authenticated copies of his power of attorney or other evidence of his authority to act on behalf of the Contractor.

* U.S. GOVERNMENT PRINTING OFFICE : 1960 OF—572728—40

CONFORMED COPY

EXCERPTED PARAGRAPHS FROM GENERAL CONDITIONS OF CONTRACT

[Exhibit No. 1 to Affidavit of Ernest R. Stacey]

7. PAYMENTS TO CONTRACTOR (1964 JUN)

(The last two sentences of paragraph (c) of the following clause are applicable only where the contract amount exceeds $1,000,000 and the time of performance exceeds one year.)

(a) The Government will pay the contract price as hereinafter provided.

(b) The Government will make progress payments monthly as the work proceeds, or at more frequent intervals as determined by the Contracting Officer, on estimates approved by the Contracting Officer. If requested by the Contracting Officer, the Contractor shall furnish a breakdown of the total contract price showing the amount included therein for each principal category of the work, in such detail as requested, to provide a basis for determining progress payments. In the preparation of estimates the Contracting Officer, at his discretion, may authorize material delivered on the site and preparatory work done to be taken into consideration. Material delivered to the Contractor at locations other than the site may also be taken into consideration (1) if such consideration is specifically authorized by the contract and (2) if the Contractor furnishes satisfactory evidence that he has acquired title to such material and that it will be utilized on the work covered by this contract.

(c) In making such progress payments, there shall be retained 10 percent of the estimated amount until final completion and acceptance of the contract work. However, if the Contracting Officer, at any time after 50 percent of the work has been completed, finds that satisfactory progress is being made, he may authorize any of the remaining progress payments to be made in full. Also, whenever the work is substantially complete, the Contracting Officer, if he considers the amount retained to

be in excess of the amount adequate for the protection of the Government, at his discretion, may release to the Contractor all or a portion of such excess amount. Furthermore, on completion and acceptance of each separate building, public work, or other division of the contract, on which the price is stated separately in the contract, payment may be made therefor without retention of a percentage. Where the time originally specified for completion of this contract exceeds one year, the Contracting Officer, at any time after 50 percent of the work has been completed, if he finds that satisfactory progress is being made, may reduce the total amount retained from progress payments to an amount not less than 10 percent of the estimated value of the work remaining to be done under the contract or 1½ percent of the total contract amount, whichever is the higher. In computing the total contract amount, for the purposes of the preceding sentence, the contract amount for any separate building, public work, or other division of the contract on which the price is stated separately in the contract and on which payment has been made in full, including retained percentage thereon under this clause shall be excluded.

(d) All material and work covered by progress payments made shall thereupon become the sole property of the Government, but this provision shall not be construed as relieving the Contractor from the sole responsibility, for all material and work upon which payments have been made or the restoration of any damaged work, or as waiving the right of the Government to require the fulfillment of all of the terms of the contract.

(e) Upon completion and acceptance of all work, the amount due the Contractor under this contract shall be paid upon the presentation of a properly executed voucher and after the Contractor shall have furnished the Government with a release, if required, of all claims against the Government arising by virtue of this contract, other than claims in stated amounts as may be specifically

excepted by the Contractor from the operation of the release. If the Contractor's claim to amounts payable under the contract has been assigned under the Assignment of Claims Act of 1940, as amended (31 U.S.C. 203, 41 U.S.C. 15), a release may also be required of the assignee. (ASPR 7-602.7(a) and (b))

26. FEDERAL, STATE, AND LOCAL TAXES (1971 NOV)

(a) Except as may be otherwise provided in this contract, the contract price includes all applicable Federal, State, and local taxes and duties.

(b) Nevertheless, with respect to any Federal excise tax or duty on the transactions or property covered by this contract, if a statute, court decision, written ruling, or regulation takes effect after the contract date and

(1) results in the Contractor being required to pay or bear the burden of any such Federal excise tax or duty or increase in the rate thereof which would not otherwise have been payable on such transactions or property, the contract price shall be increased by the amount of such tax or duty or rate increase, provided the Contractor warrants in writing that no amount for such newly imposed Federal excise tax or duty or rate increase was included in the contract price as a contingency reserve or otherwise; or

(2) results in the Contractor not being required to pay or bear the burden of, or in his obtaining a refund or drawback of, any such Federal excise tax or duty which would otherwise have been payable on such transaction or property or which was the basis of an increase in the contract price, the contract price shall be decreased by the amount of relief, refund, or drawback, or that amount shall be paid to the Government, as directed by the Contracting Officer. The contract price shall be similarly decreased if the Contractor, through his fault or negligence or his failure to follow instructions of the Contracting Officer, is

required to pay or bear the burden of, or does not obtain a refund or drawback of, any such Federal excise tax or duty.

(c) Paragraph (b) above shall not be applicable to social security taxes or to any other employment tax.

(d) No adjustment of less than $100 shall be made in the contract price pursuant to paragraph (b) above.

(e) As used in paragraph (b) above, the term "contract date" means the date set for bid opening, or if this is a negotiated contract, the contract date. As to additional supplies or services procured by modification to this contract, the term "contract date" means the date of such modification.

(f) Unless there does not exist any reasonable basis to sustain an exemption, the Government upon the request of the Contractor shall, without further liability, furnish evidence appropriate to establish exemption from any Federal, State, or local tax, *provided* that, evidence appropriate to establish exemption from any Federal excise tax or duty which may give rise to either an increase or decrease in the contract price will be furnished only at the discretion of the Government.

(g) The Contractor shall promptly notify the Contracting Officer of matters which will result in either an increase or decrease in the contract price, and shall take action with respect thereto as directed by the Contracting Officer. (ASPR 7-602.27)

77. PAYMENT TO CONTRACTOR (6-72)

(a) If the contract amount exceeds one million dollars Clause 7 PAYMENTS TO CONTRACTOR is modified as follows:

"Where the time originally specified for completion of this contract exceeds one year, the Contracting Officer, at any time after 50 percent of the work has been completed, if he finds that satisfactory progress is being made, may reduce the total amount retained from progress payments to an amount not less than 10 per-

cent of the estimated value of the work remaining to be done under the contract or 1½ percent of the total contract amount whichever is higher. In computing the total contract amount, for the purposes of the preceding sentence, the contract amount for any separate building, public work, or other division of the contract on which the price is stated separately in the contract and on which payment has been in full, including retained percentage thereon under this clause shall be excluded."

(b) To Clause 7 add the following sentence at the end of paragraph (b), and add paragraph (1) below:

Such payments shall be made on submission of itemized requests by the Contractor and shall be subject to reduction for overpayments or increase for underpayments on preceding payments to the Contractor.

(f) The obligation of the Government to make any of the payments required under any of the provisions of this contract shall, in the discretion of the OICC, be subject to (1) reasonable deductions on account of defects in material or workmanship, and (2) any claims which the Government may have against the Contractor under or in connection with this contract. Any overpayments to the Contractor shall, unless otherwise adjusted, be repaid to the Government upon demand.

Clause 103. WASHINGTON STATE SALES AND USE TAXES. Add the following clause:

"103. WASHINGTON STATE SALES AND USE TAXES

(a) Notwithstanding any provision of this contract to the contrary, the contract price excludes Washington sales and use taxes. If in the performance of this contract the Contractor is required to pay or bear the burden of any such tax, the Contractor upon furnishing proof thereof will be reimbursed, provided the Contractor warrants in writing that no amount of such tax was included in the contract price as a contingency reserve or otherwise. If the Contractor later obtains a refund of the tax, the amount

thereof, including any interest or penalty, shall inure to the benefit of the Government and shall be paid as directed by the Contracting Officer. The contractor shall take action, if directed by the Contracting Officer, challenging the validity of Washington sales and use taxes, in which event the contract price shall be equitably adjusted to cover the costs of such action, including any interest, penalty, and reasonable attorney fees.

(b) For purposes of this clause, the term "Washington sales and uses taxes" means any Washington Retail Sales or Use Tax that may be levied, collected or paid on tangible personal property purchased, produced, or used, including Government-furnished property, as a result of enactment into law in the State of Washington of Substitute House Bill No. 86.

(c) The Contractor shall insert this clause, including this paragraph (c), in all subcontracts."

IN THE UNITED STATES DISTRICT COURT FOR THE
WESTERN DISTRICT OF WASHINGTON

CIVIL ACTION NO. C77-355V

AFFIDAVIT OF JAMES F. WALSH

UNITED STATES OF AMERICA,

Plaintiff,

v.

STATE OF WASHINGTON, et al.,

Defendants.

COUNTY OF KING)
) ss.
STATE OF WASHINGTON)

JAMES F. WALSH, being of lawful age and duly sworn, deposes and says:

That I am an attorney employed as District Counsel, U.S. Army Corps of Engineers, Seattle District. I have served in this capacity since 1968. Based upon my personal knowledge of the facts of this case, the following facts are, to the best of my knowledge and belief, true:

(1) The U.S. Army Corps of Engineers is charged with flood control and flood protection of those areas west of the Continental Divide to the Pacific Ocean and generally north of the Columbia River, covering parts of the States of Washington, Idaho and Montana. My responsibility is to insure that the Contracting Officer and the District Engineer are provided with adequate legal advice on all matters relating to Army Corps of Engineers activities in this area.

(2) One such flood control and protection project is the structural modification and installation of a powerhouse housing eleven additional turbines at Chief Joseph Dam on the Columbia River in the State of Washington.

(3) Construction by the Army Corps of Engineers is accomplished by a number of prime contractors. Attached hereto as Plaintiff's Exhibit (2) is a true copy of the general provisions of one of these contracts, Contract DACW67-76-C-0043 (hereafter referred to as Contract 76-C-0043) awarded to KIEWIT-STANDARD for the construction of Pool Raising Structural Modifications to Chief Joseph Dam. The provisions of Exhibit (2) are representative of all construction contracts awarded by the Army Corps of Engineers in the State of Washington during the period involved in this litigation.

(4) Contract 76-C-0043 calls for increasing the elevation of Chief Joseph Dam. Pursuant to the terms of this contract, KIEWIT-STANDARD will procure substantial quantities of construction and building materials and building system equipment (electrical, mechanical, etc.) for incorporation into the structure.

(5) Some Army Corps of Engineers construction contracts also call for the installation and, in some cases, the testing of considerable quantities of Government-furnished property. This property may be in the form of building materials, for example, recently, during a time when it was difficult to obtain structural steel, the United States obtained large quantities of steel and furnished it to its contractor in connection with the construction of the powerhouse at Chief Joseph Dam. Exhibit (2) in its general provisions is also representative of such contracts.

(6) Government-furnished property may have been procured by the Government either within or without the State of Washington.

(7) As noted above in paragraph (3), Exhibit (2) is representative of all Army Corps of Engineers construction contracts. Exhibit (2) is a "lump-sum fixed-price" contract utilizing basic standard United States General Services Administration (GSA) provisions (Standard Forms 19-A and 23-A). Other provisions include those required by the Armed Services Procurement Regulations (ASPR). Exhibit (2) in Clause 74 includes a provision which requires Washington sales and use taxes to be

excluded from the contract price and billed separately to the Government. Clause 74 further provides that any refund of such tax will inure to the benefit of the Government. Contracts entered into prior to the effective date of the amendments to the Washington Sales and Use Tax Act which do not contain Clause 74 have been or will be modified to include substantially the same language as Clause 74 which will be applicable to all adjustments in contract price which may be later negotiated by the contract parties.

(8) Attached hereto as Plaintiff's Exhibits 3, 4, 5, and 6, respectively, are documents which have come to my attention in performing the duties of my employment and which I believe to be true copies:

(a) State of Washington Department of Revenue Excise Tax Bulletin ETB 496.08.170, issued June 6, 1975, entitled "Contractors for the Federal Government and Housing Authorities."

(b) A State of Washington Department of Revenue analysis of SHB 86 captioned "Request Number 1 (revised)," submitted April 16, 1975, consisting of two pages.

(c) Memorandum dated January 13, 1975, from Scott Morgan, Research Analyst to Representative Robert W. Randall; Committee Members, Ways and Means—Revenue re "House Bill 86 Imposing Sales Tax on Federal Government Contractors," consisting of five pages including a section-by-section digest of draft HB 86."

(d) Memorandum dated July 17, 1975, from Eleanor Brand, Research Analyst to Senator Hubert F. Donohue re "$9 million problem with HB 86 — Federal Contractors sales tax" consisting of five pages including attachment.

Subscribed and sworn to before me
this 23rd day of June, 1976.

/s/ _____
JAMES F. WALSH

/s/ _____
Notary Public

[SEAL]

My commission expires May 21, 1977.

[Exhibit No. 2 to Affidavit of James Walsh] #5(c)(2)

STANDARD FORM 23
JANUARY 1961 EDITION
GENERAL SERVICES ADMINISTRATION
FED PROC REG (41 CFR) 1-16 401

CONSTRUCTION CONTRACT

(See instructions on reverse)

CONTRACT NO. DACW67-76-C-0043
DATE OF CONTRACT

NAME AND ADDRESS OF CONTRACTOR
Peter Kiewit Sons' Co. and
Standard Construction Company, Inc.
a joint venture d/b/a
KIEWIT-STANDARD
1000 Kiewit Plaza
Omaha NB 68131

CHECK APPROPRIATE BOX
- ☐ Individual
- ☐ Partnership
- ☒ Joint Venture
- ☒ Corporation, incorporated in the States of Nebraska & Georgia

DEPARTMENT OR AGENCY
DEPARTMENT OF THE ARMY
Seattle District, Corps of Engineers
4735 East Marginal Way South, Seattle, Washington 98134

CONTRACT FOR (*Work to be performed*)
Pool Raising Structural Modifications

PLACE
Chief Joseph Dam
Columbia River, Washington

CONTRACT PRICE (*Express in words and figures*)
Seventy Million, Six Hundred Twenty-six Thousand,
One Hundred Fifty-six and Forty Hundredths Dollars ($70,626,156.40)

ADMINISTRATIVE DATA (*Optional*)

	Disbursing Officer
PAYMENT TO BE MADE BY:	Seattle District, Corps of Engineers 4735 East Marginal Way South, Seattle, Washington 98134
CONTRACT AUTHORIZED BY:	10 U.S.C. 2304(a) and Applicable Appropriation Acts
APPROPRIATION NO.:	BF 285 04 18PO 1590; BF 285 50 10N 1590

The United States of America (hereinafter called the Government), represented by the Contracting Officer executing this contract, and the individual partnership, joint venture, or corporation named above (hereinafter called the Contractor), mutually agree to perform this contract in strict accordance with the General Provisions and the following designated specifications, schedules, drawings, and conditions: Specifications, Serial No. DACW67-75-B-0045, dated 75MAR21; amendments 1 through 23 thereto; dated 75APR09, 75MAY08, 75MAY16, 75MAY28, 75JUN03, 75JUN17, 75JUL02, 75JUL11, 75JUL23, 75AUG05, 75AUG13, 75AUG19, 75SEP19, 75OCT06, 75DEC14, 75DEC17, 75DEC23, 75DEC24, undated, 76JAN20, 76FEB06, 76FEB06, & 76FEB10 respectively; Drawings as listed in Paragraph SP-5 of the specifications and Contract Schedule "A".

WORK SHALL BE STARTED	WORK SHALL BE COMPLETED
within fifteen (15) calendar days of receipt of notice to proceed.	within time stated in Paragraph SP-1 of the specifications.

Alterations: **The following alterations were made in this contract before it was signed by the parties hereto:**

Attached hereto and made a part hereof are pages 1 through 23 (Const. Gen. Prov.) (16 Oct 72 edition) (as revised).

INSTRUCTIONS

1. The full name and business of the Contractor must be inserted in the space provided on the face of the form. The Contractor shall sign in the space provided above with his usual signature and typewrite or print his name under the signature.

2. An officer of a corporation, a member of a partnership, or an agent signing for the Contractor shall place his signature and title after the word "By" under the name of the Contractor. A contract executed by an attorney or agent on behalf of the Contractor shall be accompanied by two authenticated copies of his power of attorney or other evidence of his authority to act on behalf of the Contractor.

U.S. GOVERNMENT PRINTING OFFICE 1960 OF—572726—40

In witness whereof, the parties hereto have executed this contract as of the date entered on the first page hereof.

THE UNITED STATES
OF AMERICA

By /s/ _____
RAYMOND J. EINEIGL
Colonel, Corps of Engineers
Contracting Officer

CONTRACTOR
PETER KIEWIT SONS' CO. (sponsor)

By /s/ _____

Title /s/ _____

STANDARD CONSTRUCTION COMPANY, INC.

By /s/ _____

Title /s/ _____

EXCERPTED PARAGRAPHS FROM CONSTRUCTION GENERAL PROVISIONS

[Exhibit No. 2 to Affidavit of James Walsh]

7. PAYMENTS TO CONTRACTOR (1964 JUN)

(The last two sentences of paragraph (c) of the following clause are applicable only where the contract amount exceeds $1,000,000 and the time of performance exceeds one year)

(a) The Government will pay the contract price as hereinafter provided.

(b) The Government will make progress payments monthly as the work proceeds, or at more frequent intervals as determined by the Contracting Officer, on estimates approved by the Contracting Officer. If requested by the Contracting Officer, the Contractor shall furnish a breakdown of the total contract price showing the amount included therein for each principal category of work, in such detail as requested, to provide a basis for determining progress payments. In the preparation of estimates the Contracting Officer, at his discretion, may authorize material delivered on the site and preparatory work done to be taken into consideration. Material delivered to the Contractor at locations other than the site may also be taken into consideration (1) if such consideration is specifically authorized by the contract and (2) if the Contractor furnishes satisfactory evidence that he has acquired title to such material and that it will be utilized on the work covered by this contract.

(c) In making such progress payments, there shall be retained 10 percent of the estimated amount until final completion and acceptance of the contract work. However, if the Contracting Officer, at any time after 50 percent of the work has been completed, finds that satisfactory progress is being made, he may authorize any of the remaining progress payments to be made in full. Also, whenever the work is substantially complete, the Contracting Officer, if he considers the amount retained to be in excess of the amount adequate for the protection of

the Government, at his discretion, may release to the Contractor all or a portion of such excess amount. Furthermore, on completion and acceptance of each separate building, public work, or other division of the contract, on which the price is stated separately in the contract, payment may be made therefor without retention of a percentage. Where the time originally specified for completion of this contract exceeds one year, the Contracting Officer, at any time after 50 percent of the work has been completed, if he finds that satisfactory progress is being made, may reduce the total amount retained from progress payments to an amount not less than 10 percent of the estimated value of the work remaining to be done under the contract or 1½ percent of the total contract amount, whichever is the higher. In computing the total contract amount, for the purposes of the preceding sentence, the contract amount for any separate building, public work, or other division of the contract on which the price is stated separately in the contract and on which payment has been made in full, including retained percentage thereon under this clause shall be excluded.

(d) All material and work covered by progress payments made shall thereupon become the sole property of the Government, but this provision shall not be construed as relieving the Contractor from the sole responsibility for all material and work upon which payments have been made or the restoration of any damaged work, or as waiving the right of the Government to require fulfillment of all of the terms of the contract.

(e) Upon completion and acceptance of all work, the amount due the Contractor under this contract shall be paid upon the presentation of a properly executed voucher and after the Contractor shall have furnished the Government with a release, if required, of all claims against the Government arising by virtue of this contract, other than claims in stated amounts as may be specifically excepted by the Contractor from the operation of the release. If the Contractor's claim to amounts payable

under the contract has been assigned under the Assignment of Claims Act of 1940, as amended (31 U.S.C. 203, 41 U.S.C. 15), a release may also be required of the assignee. (ASPR 7-602.7(a) and (b))

35. FEDERAL, STATE, AND LOCAL TAXES (1971 NOV)

(a) Except as may be otherwise provided in this contract, the contract price includes all applicable Federal, State, and local taxes and duties.

(b) Nevertheless, with respect to any Federal excise tax or duty on the transaction or property covered by this contract, if a statute, court decision, written ruling, or regulation takes effect after the contract date, and —

(1) results in the Contractor being required to pay or bear the burden of any such Federal excise tax or duty or increase in the rate thereof which would not otherwise have been payable on such transactions or property, the contract price shall be increased by the amount of such tax or duty or rate increase, *provided* the Contractor warrants in writing that no amount for such newly imposed Federal excise tax or duty or rate increase was included in the contract price as a contingency reserve or otherwise; or

(2) results in the Contractor not being required to pay or bear the burden of, or in his obtaining a refund or drawback of, any such Federal excise tax or duty which would otherwise have been payable on such transactions or property or which was the basis of an increase in the contract price, the contract price shall be decreased by the amount of the relief, refund, or drawback, or that amount shall be paid to the Government, as directed by the Contracting Officer. The contract price shall be similarly decreased if the Contractor, through his fault or negligence or his failure to follow instructions of the Contracting Officer, is required to pay or bear the burden of, or does not obtain a refund or drawback of, any such Federal excise tax or duty.

(c) Paragraph (b) above shall not be applicable to social security taxes or to any other employment tax.

(d) No adjustment of less than $100 shall be made in the contract price pursuant to paragraph (b) above.

(e) As used in paragraph (b) above, the term "contract date" means the date set for bid opening, or if this is a negotiated contract, the contract date. As to additional supplies or services procured by modification to this contract, the term "contract date" means the date of such modification.

(f) Unless there does not exist any reasonable basis to sustain an exemption, the Government upon the request of the Contractor shall, without further liability, furnish evidence appropriate to establish exemption from any Federal, State, or local tax, *provided* that, evidence appropriate to establish exemption from any Federal excise tax or duty which may give rise to either an increase or decrease in the contract price will be furnished only at the discretion of the Government.

(g) The Contractor shall promptly notify the Contracting Officer of matters which will result in either an increase or decrease in the contract price and shall take action with respect thereto as directed by the Contracting Officer. (ASPR 7-103.1(a))

74. WASHINGTON STATE SALES AND USE TAXES

(a) Notwithstanding any provisions of this contract to the contrary, the contract price excludes Washington sales and use taxes. If in the performance of this contract the Contractor is required to pay or bear the burden of any such tax, the Contractor upon furnishing proof thereof will be reimbursed; provided the Contractor warrants in writing that no amount of such tax was included in the contract price as a contingency reserve or otherwise. If the Contractor later obtains a refund of the tax, the amount thereof, including any interest or penalty, shall inure to the benefit of the Government and shall be paid as

directed by the Contracting Officer. The Contractor shall take action directed by the Contracting Officer, and the contract price shall be equitably adjusted to cover the costs of such action, including any interest, penalty, and reasonable attorney fees.

(b) For purposes of this clause, the term "Washington sales and use taxes" means any Washington Retail Sales or Use Tax that may be levied, collected or paid on tangible personal property purchased, produced, or used, including Government-furnished property, as a result of enactment into law in the State of Washington of Substitute House Bill No. 86 and subsequent bills relating thereto.

(c) The Contractor shall insert this clause, including this paragraph (c), in all subcontracts.

[Exhibit No. 3 to Affidavit of James Walsh]

STATE OF WASHINGTON DEPARTMENT OF REVENUE
EXCISE TAX BULLETIN

ETB 496.08.170 **Issued June 6, 1975**

CONTRACTORS FOR THE FEDERAL GOVERNMENT AND HOUSING AUTHORITIES

Effective July 1, 1975 persons performing contracts, whether as prime or subcontractors, for construction, decorating, repair, or improvement of buildings for

a. the federal government, its agencies, or instrumentalities

b. city or county housing authorities created under Ch. 35.82 RCW are subject to

1. business tax at the rate of .0044 on the gross contract price; this is to be reported as "government contracting" on line 15 of the excise tax return, the same line used for "public road construction" business tax

and such contractors are required to pay

2. sales tax (or use tax) on all purchases of materials.

Heretofore contractors performing construction contracts for the Federal Government or housing authorities have been subject to business tax as sellers. They were not required to pay sales tax on their purchases

because those purchases were for resale and their sales were also sales tax exempt because of the exempt status of the buyer. Substitute House Bill 86 was enacted as Chapter 90, Laws of 1975, 1st Ex. Sess. on May 27, 1975, to amend the statutory definition of "sale at retail" or "retail sale" to specifically exclude such construction contract work and to make such contractors consumers. The net effect of this amendatory act is to make all income from Federal or housing authority construction contracts subject to the same rate of business and occupation tax as before but under a new classification and to make such contractors liable for sales tax or use tax on all of their purchases of materials in performing such contracts.

The new law also amends RCW 82.04.190 to define as a "consumer" those persons who construct, repair, decorate or improve new or existing buildings or structures of or for the United States or housing authorities. Also included as "consumers" are persons who install or attach articles of tangible personal property in or to such buildings or structures.

Thus, retail sales tax applies upon the sale to such contractors of materials including prefabricated and precast items, equipment, fixtures and supplies consumed in the performance of such contracts.

Use tax also applies to the use of any articles produced or manufactured by contractors for their own use in performing such contracts and Manufacturing business tax is due upon the value of such articles (see Rule 134).

The provisions of the amendatory act are effective as of July 1, 1975. However, in respect to contracts executed before July 1, 1975, or contracts bid upon before July 1, 1975, but awarded after that date, contractors who would bear any additional tax burden because of the act's provisions, which additional burden is not compensable by the Federal Government, are excused from payment of the additional tax amount.

NOTE: Sales to the federal government or housing authorities continue to be sales tax exempt as before. It is sales of materials to their contractors which are made subject to sales tax by the change in the law.

[Exhibit No. 4 to Affidavit of James Walsh]

Department of Revenue	140	Concerning	SHB 86
Responding Agency Title	Code No.	SB NO.	HB NO.

Mark McLaughlin, Senate Ways and Means

Title of Bill: An Act Relating to . . . revenue and taxation

ESTIMATED STATE FISCAL IMPACT OF PROPOSED LEGISLATION

Revenue Impact by Fund and Source:	BIENNIAL IMPACT FIRST YEAR Increase (Decrease)	BIENNIAL IMPACT SECOND YEAR Increase (Decrease)	BIENNIAL IMPACT TOTAL Increase (Decrease)	SIX-YEAR IMPACT Increase (Decrease)
Fund Title: General Fund				
Source Title: Sales Tax				
State	$3,000,000	$6,000,000	$9,000,000	$19,000,000
Federal				
Local	420,000	820,000	1,240,000	2,540,000
TOTAL	$3,420,000	$6,820,000	$10,240,000	$21,540,000

Expenditure Impact by Source of Funds:				
Fund Title:				
State		NONE		
Federal				
Local				
TOTAL				

Expenditure Impact Detail:

FTE Staff Years				
Salaries and Wages				
Personal Service Contracts				
Goods and Services				
Travel				
Equipment				
Employee Benefits				
Grants and Subsidies				
Debt Service				
Capital Outlay:				
Land				
Buildings				
Improvements Other Than Buildings				
TOTAL				

Attach Explanation of Estimate
(Use Form FN-2)

David W. Weig — Prepared By
Chief Economist — Title
4/16/75 — Date

Reviewed by: /s/ — Chief, Research and Statistics

Department of Revenue — Responding Agency Title
140 — Code No.
Concerning
SB NO.
SHB 86 — HB NO.

April 16, 1975
Date Submitted

Description:

This measure broadens the sales and use tax base to include construction activity performed for the U.S. Government and county or city housing authorities. This is achieved through redefining "retail sale" to specifically exclude sales or charges in respect to construction activity for the United States, any instrumentality thereof, or a county or city housing authority, and redefining "consumer." Consumer has been redefined to include persons engaged in constructing, repairing, or improving buildings for these same governmental entities. The retail sales tax would apply to the contractor solely in respect to tangible personal property incorporated into the building or structure. Labor charges will remain exempt.

A grandfather clause is incorporated in the substitute bill. Persons submitting bids or entering into contracts prior to July 1, 1975 who would be required, under the terms of the contract, to bear the burden of the additional tax, would not be required to pay such tax.

The effective date is July 1, 1975.

Fiscal Impact:

It is assumed that contractors will incorporate this tax into the cost estimates for their bids. Therefore, the Federal Government and county or city housing authorities would bear the entire burden of the tax.

The fiscal impact has been estimated on the basis of ongoing and planned construction activity of: 1) the Corps of Engineers, U.S. Department of the Army, 2) Bureau of Reclamation, United States Department of Interior, 3) the Atomic Energy Commission, 4) the largest single construction activity, the Trident Support Site, United States Department of the Navy, and 5) selected housing authorities.

Housing authority construction within the state has been indicated to be totally funded by the U.S. Department of Housing and Urban Development.

The revenue estimates provided herein should be considered minimum revenue estimates for the six-year impact. Future federal governmental investment in energy development, plus irrigation systems, should be substantial as energy and food are generally in scarce supply.

[Exhibit No. 5 to Affidavit of James Walsh]

January 13, 1975

TO: Representative Robert W. Randall
Committee Members, Ways and Means — Revenue

FROM: Scott Morgan, Research Analyst

SUBJECT: House Bill 86 Imposing Sales Tax on Federal Government Contractors

House Bill 86 imposes state and local sales and use taxes on materials incorporated into Federal Government construction projects.

Under current law, contracted labor and materials on Federal construction projects are not subject to sales and use tax. This exclusion is attributable to two factors: 1. The state is prohibited from taxing the Federal Government and 2. The legal incidence of the Washington State sales tax falls upon the consumer, the Federal Government. Further, city and county housing authorities are exempt from all taxes and special assessments pursuant to RCW 35.83.

An example of the exclusion is as follows: Pipe purchased from a material man by a plumbing subcontractor is a sale for resale, not subject to tax. The fulfillment of the subcontract (including materials) by the subcontractor to the prime contractor can as well be considered a sale for resale, not subject to tax. The prime contractor's subsequent sale to the Federal Government is considered the final sale on which the sales tax is applicable. But, because the state is prohibited from levying taxes against the Federal Government, labor charges and materials incorporated into the project are free from sales tax.

Definitional changes to "retail sales" and "consumer" in HB 86 would subject materials to sales and use tax, payable by the construction contractor. Tax incidence on

charges for labor are unaffected by the change and will remain untaxable. Materials purchased by subcontractors are not affected, as they are considered goods for resale and thus free from retail sales tax. The draft does not affect materials purchased by supply-type contractors of the Federal Government.

City and county housing authorities have been included in the draft to maintain consistency with the Federal Government. Pursuant to RCW 35.82.210, these local housing authorities are exempt from all state and local taxes. By including local housing authority contractors within the definitional changes, virtually all materials on any construction project, be it Federal, State, local or private, are subject to sales tax.

The effect of the proposal on housing authorities is to raise the contractor's costs of operation which will ultimately be passed on to the housing authority. Either these increased costs will be passed on to low income tenants through increased rent, or the additional cost to the authority must be made up through increased revenue, from Federal or other sources. The impact on a unit built at a cost of $20,000, assuming 20% of cost attributable to materials is $200.

The impact will be similar in the case of Federal Government Contractors, where contractor's operating costs will increase, ultimately passed on to the Federal Government entity contracting for the project.

The proposal also imposes use tax on such materials when the retail sales tax has not been paid, even though title to such property may later be transferred to the Federal Government. This is to prevent any avoidance of the sales tax by direct title vesting in the Federal Government. If such provision were not allowed for, title vesting clauses could be written into all contracts. The result being to tax revenues to state or local government resulting from enactment of this proposal.

The point at which the tax applies is the point of purchase. For local tax purposes the .5% will be collected by

the county in which the purchase is made. The state and local use tax are applicable on construction materials purchased out of state and on which no tax has been collected by the state in which the goods are purchased. Following are a few examples:

A. The local taxes on materials purchased by a contractor in King County for installation in Kitsap County are collectible by King County.

B. The local use tax on materials purchased in Oregon for installation in Kitsap County will be collectible by Kitsap County.

C. In instances where materials are purchased in a state where sales tax is applied a credit on Washington use tax is granted, with state and locals collecting the difference between the originating state rate and the Washington rate.

Differential Treatment of Construction Contractors

The effect of the proposed legislation would be classification of construction contractors into two categories for determination of incidence of sales tax.

1. Conventional Contractors, those constructing and repairing new or existing buildings or other structures upon real property of private individuals as well as property of state and local governments. Further, this category includes public road contractors who construct or repair streets or roads owned by the State of Washington. The sales tax is applied against the full contract price (including materials and labor charges) and payable by the purchaser.

2. Public Road, Federal Government and Local Housing Authority Contractors. Included within this category are those building, repairing or improving streets, roads, etc., which are owned by a municipal corporation, or political subdivision of the state or by the United States. Because of ex-

isting and proposed statutory definitions, the retail sale occurs when the contractor purchases materials to be incorporated into the project. It is upon this sale that sales tax is collectible from the contractor. Unlike (1) above, only materials are subject to the tax while charges for labor remain untaxable. Passage of the proposal would add Federal Government and local housing authority construction contractors.

The State Supreme Court has ruled that the Legislature has broad flexibility in designating classifications for purposes of taxation. However, reasonable justification is a primary requirement in such designations. Consideration must be given to treatment of government contractors versus treatment of other general contractors, and whether enactment of this proposal unduly discriminates against the Federal Government and its contractors.

In other states the sales tax status of construction materials varies considerably. A number of states tax all purchases of contractors. Many tax or exempt materials for federal projects where they are taxable or exempt to state and local governments. A number of states make provisions recognizing an exempt status where the contractor is designated as the agent of the Federal Government.

Major construction projects affected by the proposal include the Trident Support Site and powerhouse construction at both Grand Coulee and Bonneville Dams. Total construction costs at the Trident site are estimated at $550 million, one-half of which is attributable to materials purchased. Construction costs at Bonneville are estimated to range between $300 million and $400 million.

The imposition of the sales and use taxes on existing contracts could adversely impact the construction contractor. The effective date applies to the date when materials purchased, not the date when the contract was entered into. Where the contractor could add the tax on as a increase in his costs of materials in contracts entered into after the effective date, the same opportunity is most likely

unavailable for those contractors purchasing materials in fulfilling a contract entered into before the effective date. In the latter case, the contractor will be left in the position of absorbing the additional tax impact if the contract cannot be altered to reflect the additional tax.

The fiscal impact is estimated to be $13.3 million over the 75-77 biennium, $1.3 million of which is collectible by local governments.

Following is a section by section digest of draft HB 86:

Section 1 — Amending 82.04.050 — Defining "sale at retail", "retail sale".

An additional paragraph defines "retail sale" to *exclude* the sale of materials and charges for labor, land clearing and earth moving to the Federal Government, its intrumentalities, and city and county housing authorities.

The effect of the definition change is to say that no retail sale (taxable event) takes place on the transfer of materials or labor charges to the Federal Government or local housing authorities.

Section 2 — Amending 82.04.190 — Defining "consumer".

RCW 82.04.190 is broken out into 4 subsections defining "consumer".

(1). "Any person who purchases, acquires, owns, holds or uses any article of tangible personal property".

(2). Includes those taxes pursuant to RCW 82.04.290, a "catch all" section which encompasses categories not specifically outlined in other sections.

(3). Public Road Contractors for U.S. Government and local governments in respect to personal property incorporated into such publicly owned road construction project.

(4). Any person who has right of possession to real or personal property being constructed, *except* U.S. Government and local governments in respect to

labor rendered to real property held for public road purposes.

The proposed amendments would alter the above subsections in the following manner:

Subsections (1), (2) and (3) remain intact.

Subsection (4) is reworked leaving local governments, in respect to labor charges on public road projects, excluded from the definiton of "consumer". The United States, its intrumentalities and local housing authorities are excluded from the definition in all respects. Language is stricken which previously excluded the U.S. Government in respect to public road construction.

Subsection (5). Where the United States and city and county housing authorities were excluded from the definition of "consumer" in (4), the contractor on such projects is now held to be the "consumer" in respect to the tangible personal property purchased for installation into the construction project.

The effect of sections 1 and 2 is to single out transfers of tangible personal property to the United States, and local housing authorities (tax exempt entities), and redefine terms to allow imposition of the sales tax on the sale to, or use tax on the use by contractors (taxable entities).

Section 3 — Amending 82.04.280 — Imposing Business and Occupation Tax.

For purposes of B & O taxation, an additional subsection is added to RCW 82.04.280 to treat Federal Government and local housing authority contractors in the same manner as local government public road contractors (2). Contractors now pay business and occupation tax at the rate of .44% under the retailing classification. Because of definition changes in sections 1 and 2, sales by contractors to these governmental entities would no longer be considered retail sales. An additional classification must be made for B & O tax purposes. The .44% rate paid by these construction contractors is *not* changed.

Section 4 — Declaring an emergency and an effective date of July 1, 1975.

[Exhibit No. 6 to Affidavit of James Walsh]

MEMORANDUM July 17, 1975

TO: Senator Hubert F. Donohue

FROM: Eleanor Brand, Research Analyst

RE: $9 Million problem with HB 86 — Federal Contractors sales tax

We were informed Wednesday, July 15, that a problem had been discovered in HB 86, creating a loophole whereby federal contractors could avoid the sales tax and thus nullify the effect or intent of the entire bill. The loophole cited is that of imposing the tax in cases where the materials are not purchased by the contractor but are supplied by the government.

The bill as currently constructed speaks to the imposition of the use tax and of value determined for the use tax in cases of bailment (use of property owned by the government), but the bill does not now speak to the possibility of use of materials which become an integral part of a building or other realty owned by the government.

The attached draft has been prepared by the House Ways and Means and has been carefully reviewed by the Revenue Department. Representative Randall intends to prefile the bill today, and is hoping that the up-coming session will address the question and make the proposed corrections.

In addition, it appears fairly certain that the bill, regardless of whether the correction is made or not, will be subject to litigation. There are indications that contractors on the Trident project and in Grand Coulee are planning to challenge the new statute. Revenue is apparently hoping that the corrections proposed will be made in order to strengthen the case of the state in imposing the tax.

The draft proposes two changes: (1) Page 2, lines 7-23 establishes definitions and values for use tax purposes in

the case of government owned articles used in construction, repairing, etc. which become a part of other realty; and (2) adding language to the imposition of the sales tax — page 3, lines 27-28 — to impose the tax on articles furnished to federal contractors.

The amendments have an emergency clause to be effective immediately.

AN ACT Relating to revenue and taxation; amending section 82.12.010, chapter 15, Laws of 1961 as last amended by section 52, chapter 278, Laws of 1975, 1st ex. sess. and RCW 82.12.010; amending section 82.12.020, chapter 15, Laws of 1961 as last amended by section 10, chapter 281, Laws of 1971 ex. sess. and RCW 82.12.020; and declaring an emergency.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF WASHINGTON:

Section 1. Section 82.12.010, chapter 15, Laws of 1961 as last amended by section 52, chapter 278, Laws of 1975, 1st ex. sess. and RCW 82.12.010 are each amended to read as follows:

For the purposes of this chapter:

(1) "Value of the article used" shall mean the consideration, whether money, credit, rights, or other property, expressed in terms of money, paid or given or contracted to be paid or given by the purchaser to the seller for the article of tangible personal property, the use of which is taxable under this chapter. The term includes, in addition to the consideration paid or given or contracted to be paid or given, the amount of any tariff or duty paid with respect to the importation of the article used. In case the article used is acquired by lease or by gift or is extracted, produced, or manufactured by the person using the same or is sold under conditions wherein the purchase price does not represent the true value thereof, the value of the article used shall be determined as nearly as possible according to the retail selling price at place of use of similar products of like quality and character under

such rules and regulations as the department of revenue may prescribe.

In case the articles used are acquired by bailment, the value of the use of the articles so used shall be in an amount representing a reasonable rental for the use of the articles so bailed, determined as nearly as possible according to the value of such use at the places of use of similar products of like quality and character under such rules and regulations as the department of revenue may prescribe ((;)): PROVIDED, That in case any such articles of tangible personal property are used in respect to the construction, repairing, decorating, or improving of, and which become or are to become an ingredient or component of, new or existing buildings or other structures under, upon, or above real property of or for the United States, and instrumentality thereof, or a county or city housing authority created pursuant to chapter 35.82 RCW, including the installing or attaching of any such articles therein or thereto, whether or not such personal property becomes a part of the realty by virtue of installation, then the value of the use of such articles so used shall be determined according to the retail selling price of such articles, or in the absence of such a selling price, as nearly as possible according to the retail selling price at place of use of similar products of like quality and character or, in the absence of either of these selling price measures, such value may be determined upon a cost basis, in any event under such rules and regulations as the department of revenue may prescribe.

In the case of articles manufactured or produced by the user and used in the manufacture or production of products sold or to be sold to the department of defense of the United States, the value of the articles used shall be determined according to the value of the ingredients of such articles.

(2) "Use," "used," "using," or "put to use" shall have their ordinary meaning, and shall mean the first act within this state by which the taxpayer takes or assumes dominion or control over the article of tangible personal

property (as a consumer), and include installation, storage, withdrawal from storage, or any other act preparatory to subsequent actual use or consumption within this state;

(3) "Taxpayer" and "purchaser" include all persons included within the meaning of the word "buyer" and the word "consumer" as defined in chapters 82.04 and 82.08 RCW;

(4) "Retailer" means every person engaged in the business of selling tangible personal property at retail and every person required to collect from purchasers the tax imposed under this chapter;

(5) The meaning ascribed to words and phrases in chapters 82.04 and 82.08 RCW, insofar as applicable, shall have full force and effect with respect to taxes imposed under the provisions of this chapter. "Consumer," in addition to the meaning ascribed to it in chapters 82.04 and 82.08 RCW insofar as applicable, shall also mean any person who distributes or displays, or causes to be distributed or displayed, any article of tangible personal property, except newspapers, the primary purpose of which is to promote the sale of products or services.

Sec. 2. Section 82.12.020, chapter 15, Laws of 1961 as last amended by section 10, chapter 281, laws of 1971 ex. sess. and RCW 82.12.020 are each amended to read as follows:

There is hereby levied and there shall be collected from every person in this state a tax or excise for the privilege of using within this state as a consumer any article of tangible personal property purchased at retail, or acquired by lease, gift, repossession, or bailment, or extracted or produced or manufactured by the person so using the same, or otherwise furnished to a person engaged in any business taxable under RCW 82.04.280, subsections (2) or (7). This tax will not apply with respect to the use of any article of tangible personal property purchased, extracted, produced or manufactured outside this state until the transportation of such article has finally ended or until such article has become commingled with the general mass of property in this state. This tax shall apply to the

use of every article of tangible personal property, including property acquired at a casual or isolated sale, and including byproducts used by the manufacturer thereof, except as hereinafter provided, irrespective of whether the article or similar articles are manufactured or are available for purchase within this state. Except as provided in subdivision (2) of RCW 82.12.030, payment by one purchaser or user of tangible personal property of the tax imposed by chapter 82.08 or 82.12 RCW shall not have the effect of exempting any other purchaser or user of teh same property from the taxes imposed by such chapters. The tax shall be levied and collected in an amount equal to the value of the article used by the taxpayer multiplied by the rate of four and one-half percent.

NEW SECTION. Sec. 3. This 1975 amendatory act is necessary for the immediate preservation of the public peace, health and safety, the support of the state government and its existing public institutions, and shall take effect immediately.

IN THE UNITED STATES DISTRICT COURT FOR THE
WESTERN DISTRICT OF WASHINGTON

CIVIL ACTION NO. C77-355V

SECOND AFFIDAVIT OF JAMES F. WALSH

UNITED STATES OF AMERICA,

Plaintiff,

v.

STATE OF WASHINGTON, et al.,

Defendants

COUNTY OF KING)
) ss.
STATE OF WASHINGTON)

JAMES F. WALSH, being of lawful age and duly sworn, deposes and says:

Based upon my personal knowledge of the facts of this case, the following additional facts are to the best of my knowledge and belief, true:

(1) Since preparing my earlier affidavit, I have been advised that construction contractors for the United States continue to be required to pay the taxes complained of in this action at least with respect to their procurement of materials for incorporation into the construction project, and insofar as I am aware, the United States has reimbursed such contractors.

(2) No other construction contractor (except the contractor for the United States and, perhaps, a county or city housing authority created pursuant to RCW chapter 35.82) pays a sales or use tax on his use of tangible personal property furnished by the owner of the property for incorporation or installation.

(3) No other construction contractor (except the contractor for the United States and, perhaps, a county or

city housing authority created pursuant to RCW chapter 35.82) pays a sales or use tax on his use of tangible personal property furnished by the owner of the property for use in respect to the construction measured by the full retail selling price, but the measure is the rental value of the property.

(4) The person who delivers a washing machine or installs it by connecting it to water and sewer and plugging it into the electricity does not pay a sales or use tax measured by the retail selling price of the washing machine; the person who paints the building does not pay a tax measured by the value of the paint or the building; and the furniture moving company or equipment installer does not pay a tax measured by the retail selling price of the shipment of household goods, office furniture, or industrial equipment he moves into the building or installs.

/s/ _____
JAMES F. WALSH

Subscribed and sworn to before me
this 5th day of January, 1977.

/s/ _____
Notary Public

My Commission expires August 14, 1980.

IN THE UNITED STATES DISTRICT COURT FOR THE
WESTERN DISTRICT OF WASHINGTON

CIVIL ACTION NO. C77-355V

DEFENDANTS' MOTION FOR
SUMMARY JUDGMENT OF DISMISSAL

UNITED STATES OF AMERICA,

Plaintiff,

v.

STATE OF WASHINGTON, et al.,

Defendants.

COME Now defendants, the State of Washington, Department of Revenue of the State of Washington, and Mary Ellen McCaffree as Director of Revenue of the State of Washington, by their undersigned attorneys and move for summary judgment in their favor, pursuant to the provisions of Rule 56 of the Federal Rules of Civil Procedure, denying the request for declaratory judgment, injunctive relief and refund of taxes made by plaintiff United States of America, and dismissing with prejudice the Complaint herein, on the grounds that there is no genuine issue as to any material fact and that the defendants are entitled to judgment as a matter of law because the Washington State tax laws which the plaintiff challenges herein are constitutionally valid. This motion is based on the pleadings and other documents filed herein.

Defendants request oral argument on this motion.

DATED this 6th day of October, 1976.

SLADE GORTON, Attorney General
State of Washington

By: /s/ _____
Richard H. Holmquist
Senior Assistant Attorney General

/s/ _____
John S. Wasberg
Assistant Attorney General
Attorneys for Defendants

UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF WASHINGTON

No. C77-355V

JOINT MOTION OF PLAINTIFF UNITED STATES OF AMERICA AND DEFENDANT STATE OF WASHINGTON FOR AMENDMENT TO COURT'S ORDER ON CROSS-MOTIONS FOR SUMMARY JUDGMENT

UNITED STATES OF AMERICA,

Plaintiff,

v.

STATE OF WASHINGTON, et al.,

Defendants.

It appearing that this Court did on the 3rd day of November, 1977, enter an order on the plaintiff's and defendants' cross-motions for summary judgment wherein this Court did deny the defendants' motion for summary judgment and did grant in part the plaintiff United States of America's motion for summary judgment, and it appearing that in this order of November 3, 1977, the Court did grant to the plaintiff United States of America certain injunctive relief against the State of Washington, and it further appearing that by this order of November 3, 1977, this Court did order the defendants to repay certain sales and use taxes which the Court held had been impermissibly collected, and it further appearing that by this order of November 3, 1977, the Court did order counsel for the parties hereto to meet and report back to the Court within 60 days of November 3, 1977, whether the parties could agree on the amount of taxes to be refunded or whether an agreement was impossible so that this Court should appoint a Special Master or take other appropriate steps to resolve this issue, wherefore the parties hereto are now reporting back to the Court and do advise the Court

that they believe an agreement can be reached as to the amount of said taxes to be refunded but that such an agreement will require extensive audits both by personnel of the plaintiff as well as personnel of the defendant State of Washington, and accordingly, the parties hereto do move the Court to amend its order of November 3, 1977, in the following respects:

1. Amend the order of November 3, 1977, to sever for separate trial proceedings the issue as to the amount of any refund of taxes from the issues concerning the constitutionality and legality of RCW 82.04, 82.08, 82.12, and 82.14, which latter issues were decided by this Court in its order of November 3, 1977;

2. Amend the order of November 3, 1977, to provide that the United States shall advise the State of Washington by March 1, 1978, as to all State sales and use taxes which it contends were impermissibly collected under this Court's order of November 3, 1977, and for which the plaintiff United States of America claims a refund; more specifically the plaintiff shall identify those taxes it has in fact either paid directly to the defendant State of Washington or has paid indirectly to the State of Washington by either reimbursing third parties who previously paid such taxes and thereafter charged the United States for said payment or instances wherein the United States made such payments to third parties for subsequent payments to the defendant; and it is further agreed that the United States shall provide the following specific information to the defendant: the amount and date of all such payments by the plaintiff United States, the identity of the persons to whom the plaintiff made the payments, and to the extent that such information is in the hands of the plaintiff, the identity of the person actually making the tax payments to the State of Washington and the dates of any such payments;

3. Amend the order of November 3, 1977, to provide that upon receipt of the foregoing information by the

defendant State of Washington, the defendant shall review such information and conduct such further audits and investigation as it deems necessary to the end that it shall report back to this Court by July 1, 1978, the results of its audit advising the Court which claims of the United States it will agree to refund and which claims it disputes, at which time this Court will consider what further trial or other proceedings may be necessary;

4. And further, in view of the four-year limitation prescribed by RCW 82.32.050 upon the right of the defendants to issue assessments for additional taxes due, and giving due consideration to the security of the rights of the defendants pending the ultimate disposition of this cause by the appellate courts of the United States, the Court acting pursuant to Rule 62(c) of the Federal Rules of Civil Procedure hereby modifies the injunction heretofore entered by the Court on November 3, 1977, as follows: During the pendency of any appeal of the injunction heretofore entered, defendants may issue assessments on the amount of the subject sales and use taxes which would have been due and payable under the challenged State statutes were such statutes constitutionally valid, but only with respect to such otherwise taxable transactions or activities as occurred prior to November 3, 1977, and only if such assessments provide that the date upon which the tax shall be due and payable is 120 days following the rendition of a decision upholding the constitutional validity of the challenged State Statutes by the United States Court of Appeals for the Ninth Judicial Circuit, or thereafter by the United States Supreme Court if appeal be had to that Court.

DATED this 30th day of December, 1977.

Respectfully submitted,

SLADE GORTON, Attorney General
State of Washington

By: /s/ _____

RICHARD H. HOLMQUIST
Senior Assistant Attorney General

Attorneys for the Defendants

/s/ _____

JOHN J. MCCARTHY
Trial Attorney, Tax Division
U.S. Department of Justice
Washington, D.C. 20530

Attorney for the Plaintiff

UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF WASHINGTON

CIVIL ACTION
NO. C77-355V

NOTICE OF APPEAL

UNITED STATES OF AMERICA,

Plaintiff,

v.

STATE OF WASHINGTON; DEPARTMENT OF REVENUE OF THE STATE OF WASHINGTON; and CHARLES W. HODDE, Director of Revenue, and his successors in office,

Defendants.

Notice is hereby given that the State of Washington, the Department of Revenue of the State of Washington, and Charles W. Hodde as Director of Revenue of the State of Washington, defendants above named, hereby appeal to the United States Court of Appeals for the Ninth Circuit from the order enjoining defendants from assessing or collecting state sales or use taxes on federal construction project contractors pursuant to provisions of Revised Code of Washington chapters 82.04, 82.08, 82.12 and 82.14 which order was entered in this action on the 3rd day of November, 1977 and modified *pendente lite* pursuant to Rule 62(c) of the Federal Rules of Civil Procedure by order entered on the 30th day of December, 1977.

DATED this 30th day of December, 1977.

SLADE GORTON, Attorney General
State of Washington

By: /s/ _____
RICHARD H. HOLMQUIST
Senior Assistant Attorney General
State of Washington
Of Attorneys for Defendants

SUPREME COURT OF THE UNITED STATES

No. 81-969

WASHINGTON, et al.,

Appellants,

v.

UNITED STATES

APPEAL from the United States Court of Appeals for the Ninth Circuit.

The statement of jurisdiction in this case having been submitted and considered by the Court, in this case probable jurisdiction is noted.

May 17, 1982

Motion to Dismiss or Affirm

Office - Supreme Court, U.S.
FILED
JAN 26 1982
L. STEVAS,
CLERK

No. 81-969

In the Supreme Court of the United States

OCTOBER TERM, 1981

STATE OF WASHINGTON, ET AL., APPELLANTS

v.

UNITED STATES OF AMERICA

ON APPEAL FROM THE
UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

MOTION TO AFFIRM

REX E. LEE
Solicitor General

GLENN L. ARCHER, JR.
Assistant Attorney General

DAVID ENGLISH CARMACK
JOHN J. MCCARTHY
Attorneys

Department of Justice
Washington, D.C. 20530
(202) 633-2217

QUESTION PRESENTED

Whether Washington sales and use taxes imposed on federal construction project contractors in the state unconstitutionally discriminate against the United States and those with whom it deals because similarly situated contractors engaged on private construction projects and on state construction projects are not so taxed.

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In the Supreme Court of the United States

OCTOBER TERM, 1981

No. 81-969

STATE OF WASHINGTON, ET AL., APPELLANTS

v.

UNITED STATES OF AMERICA

ON APPEAL FROM THE
UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

MOTION TO AFFIRM

Pursuant to Rule 16.1 of the Rules of this Court, the United States of America moves that the judgment of the Court of Appeals for the Ninth Circuit be affirmed.

OPINIONS BELOW

The decision and order of the district court (J.S. App. C-1 to C-3) is not officially reported. The opinion of the court of appeals (J.S. App. A-1 to A-15) is reported at 654 F.2d 570.

JURISDICTION

The judgment of the court of appeals was entered on August 24, 1981 (J.S. App. B-1). The notice of appeal was filed on November 13, 1981 (J.S. App.

F-1 to F-3). The jurisdictional statement was filed with the Court on November 20, 1981. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(2).

STATUTES INVOLVED

The relevant portions of chapters 82.04, 82.08, and 82.12 of the Wash. Rev. Code Ann. (1981), as amended by 1975 Wash. Laws chs. 90 and 291, § 5, and as amended 1975-1976 Wash. Laws ch. 1, are set forth at J.S. App. H-1 to H-8. The relevant portions of chapter 82.14 of the Wash. Rev. Code Ann. (1981) are set forth in the Appendix, *infra*, 1a-2a.

STATEMENT

During the period in question, the State of Washington, pursuant to chapters 82.04, 82.08, 82.12 and 82.14 of Wash. Rev. Code (1981),[1] levied a sales tax and a use tax, and authorized local counties and cities to levy sales and use taxes, on every retail sale of, and consumer use of, personal property in the state. Those taxes were required to be paid by the buyers or consumers. Prior to July 1, 1975, the sales and use tax statutes defined the terms "retail sale," "buyer" and "consumer" so that with respect to material incorporated in nonroad construction projects[2] on real property, the transaction under the prime contract between the owner of the realty and the prime contrac-

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[1] Hereinafter the Wash. Rev. Code Ann. will be cited as "RCW."

[2] Prior to July 1, 1975, RCW § 82.04.190(3) defined the term "consumer" as including a general contractor on a road-building project owned by the United States, a municipal corporation, or a political subdivision of the state, but did not include general contractors on road-building projects owned by the state or private entities.

tor constituted the only "retail sale." Furthermore, the owner of the realty was the "consumer" who had the duty to pay any sales or use tax due on the construction project. Under the statute, neither suppliers of material, subcontractors, nor the prime contractor paid any sales or use tax on the construction project or with respect to material incorporated in the building construction project. Accordingly, prior to July 1, 1975, no sales or use taxes were levied on nonroad construction projects on real property owned by the federal government in the State of Washington or on the material incorporated in such construction projects because of the immunity of the United States from state taxes under the Supremacy Clause of the United States Constitution.[3]

In an attempt to collect sales and use taxes with respect to material incorporated in building construction projects owned by the United States, the Washington Legislature in 1975 redefined the terms "retail sale" and "consumer" in its sales and use tax statutes. See (1) Substitute House Bill No. 86, enacted into law effective July 1, 1975, as 1975 Wash. Laws ch. 90;[4] (2) § 5 of Substitute Senate Bill No. 2736, enacted into law effective July 2, 1975, as 1975 Wash. Laws ch. 291, § 5;[5] and (3) House Bill No. 1229, enacted into law as 1975-1976 Wash. Laws

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[3] See *Kern-Limerick, Inc.* v. *Scurlock*, 347 U.S. 110 (1954); *M'Culloch* v. *Maryland*, 17 U.S. (4 Wheat.) 316 (1819); *First Agricultural National Bank* v. *State Tax Commission*, 392 U.S. 339, 348 (1968).

[4] This statute amended RCW §§ 82.04.050 (J.S. App. H-1) and 82.04.190 (J.S. App. H-2 to H-3).

[5] This statute also amended RCW § 82.04.050 (J.S. App. H-1).

ch. 1.[6] As a result, prime contractors performing construction work on real property owned by the United States were required to pay sales and use taxes on material and personal property incorporated into such construction projects.[7] Those statutes, however, did not amend the state's sales and use tax laws so as to impose any sales or use taxes on contractors performing construction work on real property owned by private persons or the State of Washington. With respect to those nonfederal construction projects, any sales or use taxes imposed on the project or material incorporated in the project remained the obligation of the project's owner.

Thus, prime contractors performing construction work on real property in the State of Washington were divided into two broad categories: (1) prime contractors, performing construction work for the United States and certain essentially federally financed operations of local governments, who were liable for sales and use taxes on material incorporated into the construction project; and (2) prime contractors, performing construction work for the state and private persons, who were not liable for any sales or use taxes on the project or with respect

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[6] This statute amended RCW §§ 82.12.010 (J.S. App. H-5 to H-7) and 82.12.020 (J.S. App. H-7 to H-8).

[7] The 1975 amendments also required general contractors to pay sales and use taxes on material and personal property incorporated in construction projects owned by city or county housing authorities. This change was made because the costs of these housing projects were financed by the federal government (R. 189) and because federal statutes required these projects to be exempt from state and local government taxation to qualify for federal aid. See *Housing Authority of Seattle* v. *Washington*, 629 F.2d 1307 (9th Cir. 1980); 42 U.S.C. 1437d(d). "R." refers to the record appendix in the court of appeals.

to material incorporated in the project—with any such taxes to be paid by the state or private person.

The United States thereafter commenced this suit in the United States District Court for the Western District of Washington. The suit sought: (1) a declaratory judgment that the state tax statutes were unconstitutional under the Supremacy Clause as applied to the United States and its contractors; (2) a permanent injunction enjoining the assessment and collection of those taxes from federal contractors; and (3) a judgment refunding to the United States all of the state sales and use taxes which had been collected by the state since July 1, 1975, from prime contractors engaged in construction projects on real property owned by the United States, and with respect to which the United States had reimbursed its prime contractors (J.S. App. A-6). Thereafter, the United States filed a motion for partial summary judgment seeking, *inter alia*, a declaration that chapters 82.08, 82.12 and 82.14 of the Wash. Rev. Code, Ann., as amended, unconstitutionally discriminated against the United States and its contractors, because those sales and use taxes were imposed and levied upon prime construction contractors with respect to construction projects for the United States, and were not so levied upon prime construction contractors with respect to construction projects for private individuals or the State of Washington and its various agencies (J.S. App. A-7).

The district court upheld the government's claim that the Washington sales tax unconstitutionally discriminated against contractors who deal with the United States in violation of the Supremacy Clause of the United States Constitution (J.S. App. C-1 to C-2). The district court enjoined the assessment and collection of the invalid taxes and severed the issue as

to the amount of any refund for a separate trial at a subsequent time (J.S. App. C-3). The court of appeals affirmed (J.S. App. A-14 to A-15).

ARGUMENT

The courts below correctly held that the Washington sales and use tax statutes imposed a discriminatory tax upon the contractors who dealt with the federal government and that the tax was thereby barred by the Supremacy Clause of the Constitution.

1. It is well settled that "a state tax may not discriminate against the Government or those with whom it deals." *Phillips Chemical Co.* v. *Dumas School District*, 361 U.S. 376, 387 (1960). See also *Moses Lake Homes, Inc.* v. *Grant County*, 365 U.S. 744, 751 (1961); *United States* v. *County of Fresno*, 429 U.S. 452, 464 (1977). As this Court stated in *United States* v. *City of Detroit*, 355 U.S. 466, 473 (1958), "It still remains true, as it has from the beginning, that a tax may be invalid even though it does not fall directly on the United States if it operates so as to discriminate against the Government or those with whom it deals." The proscription against taxes which discriminate against the United States or those with whom it deals is a vital element of the doctrine of the constitutional immunity of the United States from state taxation. Absent that proscription, the states could, through their taxing power, impede the functioning of the federal government. *United States* v. *County of Fresno*, *supra*, 429 U.S. at 458-462; *Montana* v. *United States*, 440 U.S. 147, 170-172 (1979) (White, J., dissenting).

The seminal decision in this area is *M'Culloch* v. *Maryland*, 17 U.S. (4 Wheat.) 316 (1819). There, the Court struck down a state tax on a national bank

as violative of the federal government's immunity to state taxation under the Supremacy Clause. In *United States* v. *County of Fresno*, *supra*, 429 U.S. at 464, this Court observed that *M'Culloch* turned on the fact that there is no political check against an abuse of a state's power to tax when the state taxes only a federal function and not its own constituents, because the state's constituents can be relied upon to vote out of office any legislature that imposes an abusive tax on them, but those constituents would not be similarly motivated when the tax is imposed solely on a federal function.

Here, the decision below correctly recognized that the Washington tax improperly discriminates against the United States and those with whom it deals. The State admits that the 1975 tax statutes in question place all construction projects in one of two categories: (1) federal construction projects and federally-financed housing authority projects [8] and cer-

[8] General contractors for city and county housing authorities were first made subject to state sales and use taxation as "consumers" on July 1, 1975, by the very same statutes which the United States is challenging in this case. These public housing authorities have been formed throughout the country pursuant to provisions of and regulations under the United States Housing Act of 1937, 42 U.S.C. 1437 *et seq.*, whereby state and local governments create these agencies to receive federal financing and grants for the purpose of providing low income housing. Federal statutes provide for annual federal contributions to these agencies providing they and their property are exempt from all real and personal property taxes, which include sales taxes levied by state and local governments. 42 U.S.C. 1437d(d). See *Housing Authority of Seattle* v. *Washington*, 629 F.2d 1307 (9th Cir. 1980). The reason that county and city housing authorities contractors were accorded the same treatment as such contractors for the United States is set forth in the legislative history of Substi-

tain public road[9] projects; (2) all other building projects, including road projects owned by the state. Thus, the state imposes sales and use taxes on federal contractors and certain local government contractors, but does not impose the same tax burden on general contractors dealing with private construction projects or with the state government.

As the court below correctly concluded (J.S. App. A-11), the fact that the private owners and the state were taxed on construction projects on their property was irrelevant. The persons similarly situated are the contractors performing construction for the federal government and the contractors working on privately or state-owned construction projects. In *County of Fresno*, this Court stated (429 U.S. at 458-459, 463) that the only protection that the United States and those with whom it deals have from abuse of state taxation on persons who deal with the United States

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tute House Bill No. 86 (R. 190). In an estimate of the fiscal impact of Substitute House Bill No. 86 dated April 16, 1975, David W. Weig, an economist, advised Mark McLaughlin of the State's Senate Ways and Means Committee that all housing authority construction in the State of Washington was totally funded by the United States Department of Housing and Urban Development (R. 188-189). Thus, it was expected that the sales tax on contractors of such housing authority projects would be passed on to the funding federal agency. It is submitted that this treatment of such housing authority contractors does not lessen the discriminatory nature of the treatment imposed upon the federal contractors.

[9] Contractors constructing roads for federal, city, and local governmental bodies (excluding the state government) were taxed prior to July 1, 1975, pursuant to RCW § 82.04.190(3). Historically such road construction projects received substantial federal financing. (See 23 U.S.C. (1952 ed.) 6; 23 U.S.C. (1964 ed.) 103, 106, 107, 120, and subsequent amendments thereto.)

is the imposition of the tax upon similarly-situated persons. Unless contractors who deal with the United States are subject to the same tax burdens as those who deal with the state and with private persons, the United States and its contractors are placed at a substantial disadvantage. See *Montana* v. *United States*, *supra*, 440 U.S. at 167-172 (White, J., dissenting). Here, the United States and the contractors dealing with the United States are at a disadvantage because similarly situated contractors dealing with private parties and the State are exempt from the sale and use taxes in question. Indeed, as the court below correctly stated (J.S. App. A-13 to A-14 n.14), the necessary political safeguard to protect the contractors who deal with the federal government from abusive tax would be present only if the contractors who deal with the private sector were similarly taxed.

The State argues (J.S. 11-13) that this Court should refine its *County of Fresno* decision to make clear that a tax only on federal contractors does not discriminate against the United States and its contractors if the tax in question merely presents to the United States the choice of reimbursing the contractor for the tax imposed upon him, thereby making him whole, or, in the alternative, refusing to reimburse so that he bears a burden no other contractors bear. But, as we have pointed out, nothing either in *County of Fresno* or in any other decision of this Court supports such a test for discrimination. And the State has failed to present any reason why the Court should depart from its well-established test.

2. Contrary to the State's further argument (J.S. 7), the decision below does not conflict with *United*

States v. *Department of Revenue of Illinois*, 371 U.S. 21, aff'g per curiam 202 F. Supp. 757 (N.D. Ill. 1962). That litigation was initiated by the United States on the ground that the Illinois retailers' occupation tax (sales tax) discriminated against the United States and those with whom it deals because the retailers' occupation tax was imposed upon persons in the state engaged in the business of selling tangible personal property at retail (including those who sold to the federal government), but was not imposed on retailers selling to the State of Illinois and its political subdivisions and to certain charitable organizations. The district court agreed with the United States that as long as the retailers dealing with the State and its political subdivisions were exempt from the occupation tax, the prohibited discrimination was present. *United States* v. *Department of Revenue of Illinois*, 191 F. Supp. 723 (N.D. Ill.), judgment vacated and remanded to consider subsequent events, 368 U.S. 30 (1961), on remand, 202 F. Supp. 757, 758, 760 (1962). On remand, the district court rejected the federal government's argument that the Illinois statute was also discriminatory because it allowed the retailer to pay the occupation tax with the use tax imposed upon private persons. 202 F. Supp. at 760.

Here, the State argues (J.S. 10-13) that the Illinois litigation permits a state to tax a federal contractor differently from other contractors. But such a reading contradicts the aspect of that decision which held that the tax was nondiscriminatory as long as Illinois imposed it on retailers dealing with the general public, the state, its political subdivisions and the United States. The source from which the retail-

ers received the money to pay the tax was irrelevant to the issue of discrimination.

Moreover, unlike the Illinois litigation, the contractors here who perform construction for the federal government on its land bear a more onerous tax burden than is imposed on contractors doing construction for the state and private persons. It is therefore clear that the Washington tax unconstitutionally discriminates against the United States and those with whom it deals.

CONCLUSION

The judgment of the court of appeals should be affirmed.

Respectfully submitted.

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JANUARY 1982

APPENDIX

Wash. Rev. Code Ann. (1981):

§ 82.14.020 [enacted by 1970 Wash. Laws ch. 94, § 3, effective Feb. 23, 1970]. *Definitions—Where retail sale occurs*

For purposes of this chapter:

(1) A retail sale consisting solely of the sale of tangible personal property shall be deemed to have occurred at the retail outlet at or from which delivery is made to the consumer;

(2) A retail sale consisting essentially of the performance of personal business or professional services shall be deemed to have occurred at the place at which such services were primarily performed;

(3) A retail sale consisting of the rental of tangible personal property shall be deemed to have occurred (a) in the case of a rental involving periodic rental payments, at the primary place of use by the lessee during the period covered by each payment, or (b) in all other cases, at the place of first use by the lessee;

(4) A retail sale within the scope of the second paragraph of RCW 82.04.050, and a retail sale of taxable personal property to be installed by the seller shall be deemed to have occurred at the place where the labor and services involved were primarily performed;

(5) "City" means a city or town;

(6) The meaning ascribed to words and phrases in chapters 82.04, 82.08 and 82.12 RCW, as now or hereafter amended, insofar as applicable, shall have full force and effect with respect to taxes imposed under authority of this chapter;

(7) "Taxable event" shall mean any retail sale, or any use of an article of tangible personal property, upon which a state tax is imposed pursuant to chapter 82.08 or 82.12 RCW, as they now exist or may hereafter be amended: *Provided, however,* That the term shall not include a retail sale taxable pursuant to RCW 82.08.150, as now or hereafter amended.

§ 82.14.030 [enacted by 1970 Wash. Laws ch. 94, § 4, effective Feb. 23, 1970]. *Sales and use taxes authorized—Maximum rates*

The governing body of any county or city while not required by legislative mandate to do so, may, by resolution or ordinance for the purposes authorized by this chapter, fix and impose a sales and use tax in accordance with the terms of this chapter. Such tax shall be collected from those persons who are taxable by the state pursuant to chapters 82.08 and 82.12 RCW, upon the occurrence of any taxable event within the county or city as the case may be. The rate of such tax imposed by a county shall be five-tenths of one percent of the selling price (in the case of a sales tax) or value of the article used (in the case of a use tax). The rate of such tax imposed by a city shall not exceed five-tenths of one percent of the selling price (in the case of a sales tax) or value of the article used (in the case of a use tax): *Provided, however,* That in the event a county shall impose a sales and use tax, the rate of such tax imposed by any city therein shall not exceed four hundred and twenty-five one-thousandths of one percent.

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Reply Brief

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No. 81-969

IN THE

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OF THE

UNITED STATES

OCTOBER TERM, 1981

STATE OF WASHINGTON, DEPARTMENT OF REVENUE OF THE STATE OF WASHINGTON, and CHARLES W. HODDE, Director of Revenue, and His Successors in Office,

Appellants,

v.

UNITED STATES OF AMERICA,

Appellee.

ON APPEAL FROM THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF OPPOSING MOTION TO DISMISS

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STATE PRINTING PLANT 3 OLYMPIA, WASHINGTON

QUESTION PRESENTED

Does the Supremacy Clause of the Federal Constitution prohibit a state from imposing a sales or use tax upon a private builder doing business with the federal government under the following circumstances:

(a) All other private builders engaged in a similar business with all other persons, including the state, its agencies and local governments, must pay a sales tax measured by the total contract price, but have the right and obligation under state law to collect that tax as reimbursement from those with whom it is doing business;

(b) Builders doing business with the federal government, on the other hand, have no such right or obligation under state law, but instead must look to the provisions of their contract with the federal government for any reimbursement of the taxes they pay?

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ARGUMENT

In its Motion to Affirm, the United States brushes aside the points raised in our Jurisdictional Statement, and rests content with the assertion—really, an *ipse dixit*—that the decision of the Court of Appeals is consistent with the two principal cases on which we rely, *United States v. County of Fresno*, 429 U.S. 452 (1977), and *United States and Olin Mathieson Chemical Corp. v. Illinois Department of Revenue*, 202 F.Supp. 757 (N.D. Ill. 1962), aff'd per curiam 317 U.S. 21 (1962). While reploughing as little old ground as possible, let us see whether this assertion is correct. We turn first to *Fresno*.

1. The result in *Fresno* rested upon a presumption, as this Court's opinion makes clear:

> "With respect to non-tax-exempt land, California imposes a property tax on the owner. No tax is imposed directly on a renter of non-tax-exempt land. However, the tax on the owner is presumably reflected in the rent and the renter may thus pay the tax indirectly." 429 U.S. at 455, note 3.

This presumption is compelled by common sense. The tax on the landlord is a cost; a landlord who could not pass his costs—including the tax—on to his tenants would not long remain in the business of being a landlord.

By reason of this presumption, the Court concluded that similarly situated tenants—both those of the United States and those of private landlords—were similarly taxed, and

> "* * * [c]onsequently, the appellants [tenants] who rent from the Forest Service are no worse off under California tax laws than those who work for private employers and rent houses in the private sector." 429 U.S. at 465.

Our argument rests upon a presumption that is identical, in all relevant respects, to that in *Fresno*. A federal contractor will recover his costs from the federal government—or he will not long remain in the contracting business. Those costs would include, of course, taxes of the sort involved in this appeal. Yet the Court of Appeals refused to give effect to this presumption or to even recognize it as legally relevant at all.

This presumption, we would agree, may not prove correct in every instance. But that does not affect our argument.

It is conceivable that, in a "buyers' market" for rental housing, a landlord may be unable to pass on all of his costs on to his tenant; he would remain in the business of being a landlord while waiting for a better day. So too with contractors. They may have to absorb temporary losses just in order to stay in business.

What is inconceivable, however, is that these economic forces would work differently for federal

contractors on the one hand and for non-federal contractors on the other. If the federal government can prevent a contractor from passing on his taxes, then for these very reasons the State, a local government, or a private buyer of construction would be able to force the contractor to bear the economic burden of *their* taxes. In short even if the presumption proves incorrect, *all* contractors would bear the economic burden of the tax and *none* would be able to pass it on.

A second point regarding *Fresno*. The United States asserts:

> "The State argues (J.S. 11-13) that this Court should refine its *County of Fresno* decision to make clear that a tax only on federal contractors does not discriminate against the United States and its contractors if the tax in question merely presents to the United States the choice of reimbursing the contractor for the tax imposed upon him, thereby making him whole, or, in the alternative, refusing to reimburse so that he bears a burden no other contractors bear. But, as we have pointed out, nothing either in *County of Fresno* or in any other decision of this Court supports such a test for discrimination. And the State has failed to present any reason why the Court should depart from its well-established test." (Motion to Affirm 9).

As we have sufficiently demonstrated already (J.S. 12, 13), the United States was put to precisely this sort of choice in *Fresno*. Thus, we are not asking that *Fresno* be *"refined,"* but simply that it be *applied*.[1]

Admittedly, the federal government may well have little real choice, as a practical matter. In order to obtain the services of private contractors, it may be required by Washington's taxing system to give up in part the

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[1]There is one issue which may have to be addressed in this case, and the resolution of which would constitute a "refinement" of *Fresno*. Is the traditional "similarly situated—similarly taxed" test, in the final analysis, different from and independent of the "political check" test established in *Fresno*? Logically, the two tests should be the same, and each produce the same legal result. But the *Fresno* opinion is not completely clear on this point.

economic advantage that it otherwise has, by reason of its constitutional immunity, over all other parties competing for the services of those same private contractors. And that, we suggest, is really the source of the federal government's complaint; it wants to keep every dollar of the economic benefit flowing from its constitutional immunity. Any system which forces it to give up some of that economic benefit has to be unconstitutional, in the view of the United States.

But a taxing system which puts the federal government to the unpalatable choice of either foregoing some of that economic benefit, by compensating the person with whom it is doing business for *his* taxes, or not doing business with that person at all, is not for that reason unconstitutional. Such a system was involved in *Fresno*, as the Court recognized. See, 429 U.S. at 464. And such a system is involved here as well.

2. A brief word concerning *Olin Mathieson*. The argument which was made by the United States in *Olin Mathieson*, and rejected, is conceptually indistinguishable from the argument which the United States makes here. Under the Illinois system, a seller to non-federal buyers had a right to collect a tax from the buyer—a use tax—and then pocket it. This resulted in that seller's having a statutory right of reimbursement from the non-federal buyer for the tax which the seller had to pay to the state. But sellers to the federal government had no right by reason of the federal government's constitutional immunity; and the United States argued that this was discriminatory.

So too here. Contractors with persons other than the federal government, *i.e.*, non-federal buyers of construction work, have a statutory right of reimbursement for the tax they must pay to the State. Contractors with the federal government don't. This difference is of no constitutional significance here, for the same reason that it was of no constitutional significance in *Olin Mathieson*.

As correctly stated by the United States:

"The source from which the retailers received the

money to pay the tax was irrelevant to the issue of discrimination." (Motion to Affirm, 10, 11).

That is precisely our point. As in *Olin Mathieson*, so too here, all sellers must pay a tax to the State. Whether they receive that money from their buyers by reason of a statutory right to reimbursement, or simply as part of the contract price, is irrelevant.

CONCLUSION

Probable jurisdiction should be noted, and the judgment of the Court of Appeals reversed.

Respectfully submitted,

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Supplemental Reply Brief

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No. 81-969

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SUPPLEMENTAL BRIEF OPPOSING MOTION TO AFFIRM

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ON APPEAL FROM THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

MOTION FOR LEAVE TO FILE AND SUPPLEMENTAL BRIEF OPPOSING MOTION TO AFFIRM

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MOTION FOR LEAVE TO FILE SUPPLEMENTAL BRIEF OPPOSING MOTION TO AFFIRM

The Appellants, State of Washington, et al., respectfully move for leave to file a supplemental brief opposing the motion to affirm previously filed by the United States. The brief is appended to this motion, and is occasioned by this Court's decision, issued March 24, 1982, in United States v. New Mexico, ___ U.S. ___ (42 CCH S.Ct. Bull. 1739). Specifically, we wish to comment briefly on note 11 of the opinion in New Mexico, as it bears upon the instant appeal.

Additionally we wish to bring to the Court's attention the "Questions Presented" in the Jurisdictional Statement of the United States in

United States and Olin Mathieson Chemical Corp. v. Ill. Department of Revenue, 202 F.Supp. 757 (N.D. Ill. 1962), aff'd per curiam 371 U.S. 21 (1962). Those Questions Presented show in a striking manner the relationship between the issues involved in Olin Mathieson and those involved here.

These two short submissions will further show why a per curiam affirmance of the Court of Appeals in the instant case will serve only to increase uncertainty as to the proper principles governing state taxation of those doing business with the federal government. Such an affirmance would mark a step backwards from the clarity achieved in this important area of constitutional law by the recent

opinions of this Court in United States v. New Mexico, supra, and United States v. County of Fresno, 429 U.S. 452 (1979).

Respectfully submitted,

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QUESTION PRESENTED

Does the Supremacy Clause of the Federal Constitution prohibit a state from imposing a sales or use tax upon a private builder doing business with the federal government under the following circumstances:

(a) All other private builders engaged in a similar business with all other persons, including the state, its agencies and local governments, must pay a sales tax measured by the total contract price, but have the right and obligation under state law to collect that tax as reimbursement from those with whom it is doing business;

(b) Builders doing business with the federal government, on the other hand, have no such right or obligation under state law, but instead must look

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SUPPLEMENTAL BRIEF OPPOSING MOTION TO AFFIRM

A. United States v. New Mexico

In United States v. New Mexico,

___ U.S. ___ (March 24, 1982, 42 CCH S.Ct. Bull. 1739) the Court stated in note 11:

> "With the abandonment of the notion that the economic--as opposed to the legal--incidence of the tax is relevant, it becomes difficult to maintain that federal tax immunity is designed to insulate federal operations from the effects of state taxation. It remains true, of course, that state taxes on contractors are constitutionally invalid if they discriminate against the Federal Government, or substantially interfere with its activities. See United States v. County of Fresno, 429 U.S. 452, 463 n. 11, 464 (1977); Moses Lake Homes, Inc. v. Grant County, 365 U.S. 744 (1961); City of Detroit v. Murray Corp., 355 U.S. 489, 495 (1958). New Mexico, however, is not discriminating here."

The Court's reference to note 11 in Fresno is especially important here. That note reads as follows:

> "A tax on the income of federal employees, or a tax on the possessory interest of federal employees in Government houses,

> if imposed only on them, could be escalated by a State so as to destroy the federal function performed by them either by making the Federal Government unable to hire anyone or by causing the Federal Government to pay prohibitively high salaries. This danger would never arise, however, if the tax is also imposed on the income and property interest of all other residents and voters of the State."

So too here, the tax involved is Washington's general sales and use tax. That tax cannot conceivably be escalated, either in its rate or in its base, so as to destroy a federal function. That danger, we submit, could never arise. (For a fuller discussion of this point, see Brief of Amicus Curiae Multistate Tax Commission in Support of Jurisdictional Statement, 16-19.)

If this submission be correct, then it should be dispositive of this

case, as suggested in note 11 of the opinion in New Mexico and note 11 of the opinion in Fresno.

B. United States and Olin Mathieson Chemical Corp. v. Ill. Dept. of Revenue.

In United States and Olin Mathieson Chemical Corp. v. Ill. Dept. of Revenue, 202 F.Supp. 757 (N.D. Ill. 1962), aff'd per curiam 371 U.S. 21 (1962), the Questions Presented as framed by the United States in the jurisdictional statement were as follows:

> "Whether, as applied to sales made to the United States, the Illinois Retailers' Occupation Tax Act is unconstitutional because--
>
> "1. it violates the immunity which the United States has from state taxation by imposing a tax upon sales made to the United States; and

"2. it discriminates against the United States and those with whom it deals in that

"a. it provides (in conjunction with the related Use Tax Act) that purchasers other than the United States will themselves pay the tax, whereas the seller must pay the tax on sales to the United States, and

"b. it exempts from the tax sales to charitable, religious and educational institutions." (Emphasis added.) (Jurisdictional Statement, 2, No. 235, O.T. 1962).

The italicized language accurately states the same discrimination issue as is involved here, and belies the assertion of the United States that the two cases can be distinguished. (Motion to Affirm, 9-11).

Respectfully submitted,

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No. 81-969

IN THE SUPREME COURT OF THE UNITED STATES

October Term, 1981

STATE OF WASHINGTON, DEPARTMENT OF REVENUE OF THE STATE OF WASHINGTON, AND CHARLES W. HODDE, Director of Revenue, and His Successors in Office,

Appellants,

v.

UNITED STATES OF AMERICA,

Appellee.

ON APPEAL FROM THE UNITED STATES COURT OF APPEALS, NINTH CIRCUIT

BRIEF ON BEHALF OF STATE OF CALIFORNIA AS AMICUS CURIAE IN SUPPORT OF APPELLANT'S JURISDICTIONAL STATEMENT

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Detroit v. Murray Corp.
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of Revenue of State of Ill.
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QUESTION PRESENTED

Does the Supremacy Clause of the Federal Constitution prohibit a state from imposing a sales or use tax upon a private builder doing business with the federal government under the following circumstances:

(a) All other private builders engaged in a similar business with all other persons, including the state, its agencies and local governments, must pay a sales tax measured by the total contract price, but have the right and obligation under state law to collect that tax as reimbursement from those with whom it is doing business;

(b) Builders doing business with the federal government, on the other hand, have no such right or obligation under state law, but instead must look to the provisions of their contract with the

federal government for any reimbursement of the taxes they pay?

* * *

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INTEREST OF THE AMICUS CURIAE

The State of California is now defending two lawsuits[1/] in federal courts

1. U.S.A. v. Cal. St. Board of Equalization, U.S.D.C., Central District of California, No. 79-03359-R (Appeal to U.S. Supreme Court pending as No. 81-1000, response by United States to Jurisdictional Statement due January 22, 1982) (involving leases to United States)); U.S.A. v. Cal. St. Board of Equalization, U.S.D.C., Central District of California, No. 81-1588-R (Appeal to Court of Appeals, Ninth Circuit filed) (sales and leases to "federal instrumentalities").

wherein the United States contends alternatively that the California sales tax (1) is unconstitutionally discriminatory and (2) unconstitutionally places the legal incidence on the United States.[2/] Here and in the California cases the United States is attacking rules developed by the court in a series of cases under which states may impose taxes on persons dealing with the United States even though the economic burden of such taxes may fall on the United States and the tax collected from those persons dealing with the United States is "complementary" to and imposed on different parties than is the tax normally collected.

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2. The legal incidence issue was determined below in favor of Washington. It is not yet known whether the United States will raise this issue before the Supreme Court. California has asked this Court for a ruling on both constitutional issues (discrimination and legal incidence) in No. 81-1000.

The two constitutional issues are interrelated, because the burden of the taxes imposed here and by California on private parties may be shifted to the United States by contract or increases in prices. This Court should either summarily reverse the decision here as unconsistent with the cases cited hereinafter or note probable jurisdiction and hear this case in tandem with No. 81-1000 to permit a thorough analysis of these important interrelated constitutional issues which affect millions of dollars (in California alone) of urgently needed state tax revenue.

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ARGUMENT

THE DECISION SHOULD BE SUMMARILY REVERSED OR PROBABLE JURISDICTION SHOULD BE NOTED BECAUSE THE DECISION BELOW CONFLICTS WITH THE POLICY AND DECISIONS OF THIS COURT

> "Today the United States does business with a vast number of private parties. In this Court the trend has been to reject immunizing these private parties from nondiscriminatory state taxes as a matter of constitutional law. . . . Wise and flexible adjustment of intergovernmental tax immunity calls for political and economic considerations of the greatest difficulty and delicacy. Such complex problems are ones which Congress is best qualified to resolve." (United States v. Detroit (1958) 355 U.S. 465, 474; emphasis added.)

In a series of cases beginning in 1937, this Court has developed the rule that,

> ". . . the economic burden on a federal function of a state tax imposed on those who deal with the Federal Government does not render the tax unconstitutional so long as the tax is imposed equally on the other similarly

situated constituents of the State." (United States v. County of Fresno (1977) 429 U.S. 452, 462.)

As a part of this same series of cases this Court has consistently upheld complementary state taxes against the charge of unconstitutional discrimination. In 1939 Southern Pacific Co. v. Gallagher 306 U.S. 167, upheld the California use tax imposed on persons exempt from the sales tax. Three cases in 1958 (United States v. Detroit 355 U.S. 466; United States v. Township of Muskegon 355 U.S. 484; Detroit v. Murray Corp. 355 U.S. 489) upheld taxes on possessory interests in and use by businesses of real property whose owners were exempt from the general property tax. In 1962 an occupation tax payable by persons selling to persons exempt

from the use tax was held not unconstitutionally discriminatory. (United States v. Department of Revenue of Illinois (1962) 371 U.S. 21, affirming per curiam a three-judge court decision 202 F.Supp. 757.) In 1977 a possessory interest tax on private individuals using governmental property exempt from the property tax normally paid by owners was upheld. (United States v. County of Fresno, supra, 429 U.S. 452.) There the court concluded,

> "There was no discrimination against the Federal Government, its property or those with whom it does business. There was no crippling obstruction of any of the Government's functions, no sinister effort to hamstring its power, not even the slightest interference with its property. Cf. M'Culloch v Maryland, 4 Wheat 316, [4 L Ed 579]. In such circumstances the Congress is the proper agency, . . . [to determine] to what extent private parties who do business with the Government should be given immunity from state taxes." (Id. at pp. 467-468.)

The lower court decision here totally ignored the ability (discussed by this Court in some of the above cases) of parties to a contract (here contractors and the United States) to shift the tax burden by adjusting prices or other arrangements. (This ability avoids tax discrimination no matter on which party the legal incidence of the tax falls.) The determination here is inconsistent with the reasoning and holdings of the above cited cases. It is diametrically in conflict with the holding approved by this Court (371 U.S. 21) which states:

> "Plaintiffs' argument on discrimination concedes that the use tax is not exacted from the federal government and it is urged by plaintiffs that a retailer who sells to the federal government must pay the occupation tax out of his own pocket because he cannot collect the use tax from the purchasing sovereign; whereas a retailer dealing with a purchaser who is not

> the federal government need not pay the occupation tax when he collects the use tax from such purchaser. This contention of 'discrimination' among retailers because of the immunity of the United States from taxation contradicts the theory urged by plaintiffs. A discrimination among taxpayers resulting from adherence to the doctrine of sovereign immunity is not only reasonable but mandatory." (United States v. Department of Revenue of State of Ill. (1962) 202 F.Supp. 757, 760.)

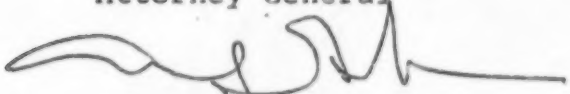
CONCLUSION

This Court has recognized that those who do business with the government must pay their fair share of taxes. To prevent the use of complementary taxes - applied to another party to a transaction where the normal taxpayer is exempt - will allow tranactions involving the federal government to completely avoid tax while all other similar transactions pay their part of the cost of government. Millions of dollars of state revenues are involved.

The lower court decision here conflicts with the past policy and rulings mentioned above of this Court. It should be summarily reversed or probable jurisdiction should be noted and the discrimination issue should be briefed and heard in tandem with No. 81-1000.

Respectfully submitted,

GEORGE DEUKMEJIAN,
Attorney General



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ON APPEAL FROM THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

MOTION FOR LEAVE TO FILE AND BRIEF OF AMICUS CURIAE MULTISTATE TAX COMMISSION IN SUPPORT OF JURISDICTIONAL STATEMENT

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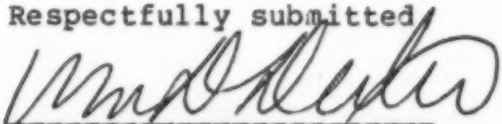
MOTION FOR LEAVE TO FILE BRIEF OF AMICUS CURIAE MULTISTATE TAX COMMISSION

The Multistate Tax Commission respectfully moves for leave to file a brief as amicus curiae in this case. The brief is appended to this motion. Consent of both the Appellants, State of Washington, et al., and the Appellee, the United States, has been obtained.

The Multistate Tax Commission is the administrative agency of the Multistate Tax Compact, entered into currently by 19 states (including Washington) and the District of Columbia as full members, and by 11 states as associate members. See, U.S. Steel Corp. v. Multistate Tax Commission, 434 U.S. 452 (1978) for a discussion of the purpose and functions of the Compact and the Commission.

The interest of the Commission in this case is the same as that of its member states and their sister states. The decision of the Court of Appeals in this case would effectively preclude the 45 states which have a sales and use tax system from imposing a vendor type sales tax upon retail sales to the federal government if that same state also imposed a vendee type sales tax upon similar sales to non-federal buyers. The Commission believes that a brief discussion of the long-run policy questions raised by this restriction will assist the Court in evaluating the importance of this case.

Respectfully submitted,



WILLIAM D. DEXTER
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Multistate Tax Commission

QUESTIONS PRESENTED

I. Is a state sales tax, the legal incidence of which falls upon the private seller of goods or services when the purchaser is the federal government, discriminatory, and accordingly invalid under the Supremacy Clause, when it is part of a state sales and use tax system under which the legal incidence of the tax falls upon the purchaser rather than the seller, when the purchaser is not the federal government?

II. Does the political check necessary, under United States v. County of Fresno, 429 U.S. 452 (1977), in order to validate a state tax upon a private seller of goods or services to the federal government, exist when the same or a similar tax is imposed upon all other purchasers of such goods or services?

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INTEREST OF AMICUS CURIAE

The concern of the Commission in this case stems from the long-run

consequences of the decision below to its member states. For reasons we shall discuss shortly, the protection afforded the federal treasury by that decision may well prove ephemeral. What is certain, however, is this: A state which wishes to obtain revenue from a transaction involving the federal government can do so, even under the decision below--but only at a very high cost. For it would require a state to restructure its sales and use tax system in a way that lessens overall efficiency in the administration of that system, and to forego policy options that are otherwise completely legitimate.

It is the Commission's interest in preserving the flexibility of the states in structuring their individual tax systems which prompts this brief in support of Washington's jurisdictional

statement.

STATEMENT

The statement of the case in the jurisdictional statement sets out the major relevant facts. A short synopsis, however, may be useful in placing Washington's sales and use tax structure in its nationwide setting.

Washington is one of the 45 states which have a general sales and use tax system.[1] As is the case in over half of these states, the Washington sales tax is a vendee, rather than a vendor type of tax.[2] That is, although the seller is required to pay the tax to the State, just as in the case of a vendor type of tax, the seller is statutorily entitled to reimbursement of that tax from the buyer.

The difference between the two

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1 All States Tax Guide, Prentice Hall, (1981), paragraph 250.

2 Ibid.

types of sales taxes is illustrated by the Washington system. The seller is required to add the tax to the sales price and collect it from the buyer. Wash.Rev.Code, § 82.08.050. Indeed, if the sales tax is not so collected from the buyer and remitted to the State, the State can itself proceed directly against the buyer, or against the seller, at the State's option. Ibid. And should the State proceed directly against the seller, the seller retains his right to reimbursement from the buyer. Ibid.

The obvious advantage of this type of sales tax to the State of Washington is that it provides the maximum assurance that the tax will be collected and remitted to the State treasury. The State need not look only to the seller for payment, but may look to the buyer as well.

In the case of ordinary sales of tangible personal property, between a private buyer and seller, this difference between a vendor and a vendee type sales tax is not as great as might first appear. This is because both types of sales taxes are invariably accompanied by a use tax, which is imposed upon the user (normally, the buyer) at the same rate as the sales tax.[3] The use tax applies unless the sales tax is paid to the State.[4] The use tax thus affords a mechanism for collection from the buyer, even if the sales tax is a vendor type tax.

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3 Ibid.

4 See, e.g., U.S. and Olin Mathieson Chemical Corp. v. Ill. Dept. of Revenue, 202 F.Supp. 757 (N.D. Ill. 1962) aff'd per curiam, 371 U.S. 21 (1962), for a discussion of the interrelationship between the Illinois use tax and the Illinois vendor type sales tax.

The difference between a vendor and vendee type of sales tax becomes critical, however, when sales to the federal government are involved. A vendor type is constitutionally permissible; a vendee type--such as Washington's--is not. See, United States v. Fresno, 429 U.S. 452, 459, note 2.

Because of this constitutional immunity, the Washington sales tax does not apply to ordinary sales of tangible personal property to the federal government. Nor did it apply, before the statutory changes involved in this case were adopted in 1975, to sales of tangible personal property to private contractors for the federal government. This is because, under Washington law, the transaction between the private contractor and the construction owner was considered a retail sale, and,

accordingly, sales of tangible personal property to the contractor, for incorporation into the construction project, were considered sales for resale, i.e., wholesale sales, and hence exempt from the sales tax.

In the case of construction for private parties and for the state and local government, the result was that the tax was imposed upon the transaction between the contractor and the construction owner, and was measured by the total cost of the construction. In the case of construction for the federal government, however, the result was markedly different; the state received no sales tax revenue from the construction at all--either from the transaction between the contractor and the federal government, or from transactions between the contractor and

his suppliers.

In an obvious effort to garner more revenues from federal construction projects, the State changed the definition of retail sale in a manner which excluded from that definition the transaction between the contractor and the federal government, but included transactions between the contractor and his suppliers. As a result of this change, the legal incidence of the tax was thus shifted from the federal government to the private contractor. The tax was not changed from a vendee to a vendor type of tax by directly eliminating the statutory right to reimbursement. But a very similar result was accomplished, by making the contractor, who had previously been the seller for sales tax purposes, now the buyer.

The statutory obligation of the

contractor to pay the sales tax remains, though the tax now has a smaller measure or base. But the contractor has lost his statutory right of reimbursement from the owner, since he has now been made a buyer instead of a seller. It is this change which precipitated the present litigation and which the court below invalidated on the grounds that it discriminated against those private contractors affected by the change.

THE QUESTIONS PRESENTED ARE SUBSTANTIAL, AND MERIT FULL REVIEW BY THE COURT.

I. Because the Decision Below Unduly Restricts the Policy Choices Available to a State in Structuring its Tax System, This Case Presents a Question of Fundamental Importance to the Proper Functioning of our Federal System.

We start with the options available to the State of Washington when it decided, in 1975, to garner more revenue from transactions between

private contrators and the federal government.

First, it could have simply turned its entire sales tax system from a vendee type of tax to a vendor type, by eliminating the statutory right of the seller to reimbursement by the buyer. The federal government would then have no complaint, either on the grounds that the incidence of the tax fell upon the federal government or on the grounds that the government's contractors, or any other sellers to the government, for that matter, were subject to any sort of discrimination. The result would be even more revenue from transactions with the federal government than Washington attempted to obtain in 1975. All ordinary sales of tangible personal property would now be taxable, and construction contracts would be taxable on the full cost,

rather than just on the cost of materials.[5]

This option would still be open to the State even if the decision below is affirmed. But note the cost of that option, in terms of equity between taxpayers and in terms of efficient administration of a tax system. The State would be required to look only to

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5 Two additional changes might be required. As noted in the jurisdictional statement, pp. 3, 4, two types of contractors are now treated in precisely the same manner as are contractors with the federal government. Those are certain public road contractors, and contractors with public housing authorities. In order to avoid any charge of discrimination against contractors with the federal government, presumably they would have to be treated the same as all other contractors. This would result, of course, in even greater revenue from the State. Indeed, it may have been the State's reluctance to increase the tax burden on public road construction projects which prompted the Washington legislature to treat contractors with the federal government in the same manner as these public road contractors.

the seller for payment, and would be foreclosed from requiring the buyer to pay in the event that the seller does not. The protection to State revenues afforded by a vendee type of sales tax would be lost.

This protection could be provided, we agree, through the imposition of the use tax upon the buyer. And under Olin Mathieson, a vendor type sales tax may be constitutionally imposed upon sales to the federal government even though it is part of a system which contains such a use tax. Administratively, when an in-state sale is involved, a use tax is equivalent to a vendee type sales tax. But for the reasons discussed in the jurisdictional statement, pp. 7-9, an affirmance of the decision of the Court of Appeals in this case would cast serious doubt upon the continuing validity of Olin Mathieson. And thus a

State which shifts to a vendor type of sales tax would probably be compelled to jettison its use tax as well, in order to reach sales to the federal government.

Secondly, Washington could have removed all contractors from its sales and use tax system, and utilized in its place another tax, i.e., its business and occupation tax. This is a gross receipts tax imposed at a relatively low rate, i.e., at .44 percent of the gross proceeds of sales. (See Wash.Rev.Code § § 82.04.220, 82.04.250.) If that rate were simply increased by the amount of the sales tax rate, the effect would be exactly the same as under the first option, but would be limited to contractors rather than extended to all sales transactions. Although this second option, which is really a limited

variation of the first, would garner more revenue from federal construction projects, since the entire amount of gross receipts would be in the tax base, the disadvantage involved in the first option would still exist with respect to non-federal construction projects.

In sum, our point is this: The flexibility of the states in structuring their tax systems should be restricted only to the extent necessary to protect the federal interest. When a court adopts restrictions beyond those necessary to protect that interest, it does more than deprive a state of the revenues it has determined it needs. Indeed there is always a way for the state to recapture that revenue and thereby repair that damage. But the court has also inflicted a permanent sort of damage; it has

damaged an integral part of our federal system itself.

That is what the Court of Appeals has done here. And to show why this is so, we next examine that federal interest more closely, guided by this Court's decision in United States v. County of Fresno, 429 U.S. 452 (1977).

II. This Case Presents an Important Question as to the Scope of the "Political Check" Doctrine as Established in United States v. County of Fresno.

The Court of Appeals disposed of the political check issue in the following passage of its opinion:

> ". . .
>
> "As to the State's second related argument, the political check that was described in Fresno simply is not present in this case. In Fresno, there was a similarly situated group that was analogously taxed, namely, the lessees of non-exempt property. That group provided the necessary political safeguard. Here

> there is no broad state constituency taxed as are the prime contractors who deal with the federal government. Only when those similarly situated not dealing with the federal government feel the same tax burden as those dealing with it, can the State's constituency be relied upon to ensure that the taxation does not rise to abusive levels. Thus, only if all prime contractors were forced either directly or indirectly to pay the challenged taxes would the political check described in Fresno be present. In that situation alone would it be clear that those with interests comparable to federal contractors could be relied upon to ensure that the tax on federal contractors would not rise to abusive levels.[Footnote omitted.]" J.S. A-13.

To show why this conclusion is wrong, we ask: How might the State of Washington, if it wanted to, actually go about raising the tax on federal contractors to "abusive levels"? One way might be to raise the rate of the tax. The tax in issue, however, is the general sales and use tax. It is the

same tax as is imposed on non-federal construction, and on almost all sales of tangible personal property as well.[6] Not only contractors and their customers, but almost every other buyer and seller of tangible personal property would be affected by a raise in the rate. A more effective political check could hardly be imagined.

The State could also, to be sure, expand the base or measure of the tax on federal contractors, while leaving the rate unchanged, and leaving, as well, the legal incidence of the tax upon those contrators. The base could be expanded from one which includes only the cost of materials and

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6 For the exemptions from the sales tax, see Wash.Rev.Code, § 82.08.0251-82.08.035. The only major exemption is for non-restaurant food items (§ 82.08.0284).

components incorporated into the construction project, which is the base now, to a base which includes the total cost of construction. And this change could, we agree, be made without any significant political check. Besides federal contractors, such a change would affect only a relatively small group of public road contractors and contractors for public housing authorities.

But this expansion would make the base for federal contractors exactly the same as it is now for all other contractors.[7] Any further efforts to raise the tax on federal contractors would necessarily involve the imposition of some other sort of tax,

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7 Our use of the phrase "all other contractors" does not include this small group of public road contractors and contractors for public housing authorities, who are now treated identically to federal contractors, and taxed, accordingly, on the smaller base.

not the tax in issue here. The general sales and use tax would have been expanded to its limit--just as has been the case for many years for non-federal construction.

With such an expansion of the base, the only difference between federal contractors and all other contractors would be that federal contractors would not have a statutory right to reimbursement, while all other contractors would. Stated otherwise, federal construction would be subject to a vendor type tax, and all other construction would be subject to a vendee type tax; but the rate and base would be identical.

For the Court of Appeals, the existence of this difference between the two types of taxes was decisive. Under the Court of Appeals' opinion, so long as that difference exists, the

necessary political check cannot exist, and the tax on the federal contractor is unconstitutional.

Logically, under that opinion the political check would not exist in any situation in which a vendor type of tax is imposed on sales to the federal government while a vendee type of tax is imposed on similar transactions with everyone else. Whether the sale involves airplane parts, as in Olin Mathieson, or construction, as here, the result would be the same; as long as the State imposes a vendee type tax, rather than a vendor type tax, on non-federal sales, the vendor type tax on federal sales must fall, for lack of the necessary political check.

Such a result is completely unjustified by Fresno. It converts the political check doctrine into a mere mechanical tool. It protects the

federal government from a danger that is non-existent, while forcing the states into a legal straight-jacket in structuring their tax systems.

This result is also completely inconsistent with the approach taken by this Court in another important area in which the charge of discriminatory state taxation has often been made, i.e., the area of interstate commerce. If, for example, a person were to purchase personal property in one state, but bring it into a second state for use there, that person could be subjected to the familiar use tax--but only if in-state purchases were taxed as well by that second state, through a sales tax. But it matters not whether that sales tax is a vendor or a vendee type of tax.

As stated in Southern Pacific Co. v. Gallagher, 306 U.S. 167 (1939):

> ". . . A discrimination against goods of out-of-state origin on the face of the sales and use acts is suggested because the local retailer may absorb the sales tax while the consumer of an imported article must pay the use tax. [Footnote omitted.] But this is not a discrimination in the law. California's exaction for the distribution of tangible personal property is the same, whether purchased within or without her borders or whether paid by the retailer or consumer. There is an equal charge against what is used, whatever its source. . . ." 306 U.S. at 172.

The same approach, with the same flexibility for the states to decide whether to impose a vendor or vendee type sales tax, should be taken here.

CONCLUSION

For the reasons given above, probable jurisdiction should be noted in this case.

Respectfully submitted,

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Multistate Tax Commission

Appellant's Brief

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QUESTION PRESENTED

Does the Supremacy Clause of the Federal Constitution prohibit a state from imposing a sales or use tax upon a private builder doing business with the federal government under the following circumstances:

(a) All other private builders engaged in a similar business with all other persons, including the state, its agencies and local governments, must pay a sales tax measured by the total contract price, but have the right and obligation under state law to collect that tax as reimbursement from those with whom it is doing business;

(b) Builders doing business with the federal government, on the other hand, have no such right or obligation under state law, but instead must look to the provisions of their contract with the federal government for any reimbursement of the taxes they pay?

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No. 81-969

IN THE

SUPREME COURT

OF THE

UNITED STATES

OCTOBER TERM, 1981

STATE OF WASHINGTON, DEPARTMENT OF REVENUE OF THE STATE OF WASHINGTON, and CHARLES W. HODDE, Director of Revenue, and His Successors in Office,
Appellants,

v.

UNITED STATES OF AMERICA,
Appellee.

ON APPEAL FROM THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

APPELLANTS' OPENING BRIEF

OPINIONS BELOW

The opinion of the U.S. Court of Appeals for the Ninth Circuit (J.S. App. A1-15) is reported at 654 F.2d 570. The decision and orders of the U.S. District Court for the Western District of Washington (J.S. Appendices C and D) and are unreported.

JURISDICTION

This appeal is taken from a judgment of the United States Court of Appeals for the Ninth Circuit affirming the order of the United States District Court for the Western District of Washington, which invalidated as unconstitutional under the Supremacy Clause (Art. VI, cl. 2) the application of Washington State sales and use tax statutes to building contractors doing business with the federal government.

Jurisdiction in the action brought by the United States in the District Court was conferred by 28 U.S.C. § 1345. Appeal of the orders entered by the District Court was timely taken by the State of Washington to the Court of Appeals pursuant to 28 U.S.C. § 1291.

The judgment of the Court of Appeals was entered on August 24, 1981, and a notice of appeal to this Court was filed in the Court of Appeals on November 16, 1981. This Court noted probable jurisdiction in the appeal by order entered May 17, 1982. Jurisdiction is conferred by 28 U.S.C. § 1254(2).

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

Federal Constitution:

U.S. Const., Art. VI, cl. 2 (Supremacy Clause) is reproduced at J.S. App. G.

State Statutes:

Washington Session Laws

1975 Wash. Laws, ch. 90, § § 1, 2, 3, 4 (SHB No. 86), amending Wash. Rev. Code § § 82.04.050, 82.04.190, 82.04.280.

1975 Wash. Laws, ch. 291, § 5 (SSB No. 2736), amending Wash. Rev. Code § 82.04.050.

1975-1976 Wash. Laws, ch. 1, § § 1, 2 (HB No. 1229), amending Wash. Rev. Code § § 82.12.010 and 82.12.020. These are reproduced at Br. App. A.

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Wash. Rev. Code § § 82.04.050, 82.04.190, 82.04.280(7), 82.08.020, 82.08.050, 82.12.010, and 82.12.020, are reproduced at J.S. App. G.

State Administrative Regulations

Wash. Admin. Code § 458-20-198 is reproduced at Br. App. B.

STATEMENT OF THE CASE

The facts necessary to a resolution of this appeal are not in dispute and are set forth here after the following summary of the procedural history of the case.

I. NATURE OF PROCEEDINGS AND JUDGMENTS BELOW

The United States commenced this litigation in February 1976 against the State of Washington, filing its complaint in the United States District Court for the Western District of Washington. (J.A. 5). The complaint sought (1) a declaratory judgment that as amended in 1975 the Washington sales and use tax in its application to construction for the United States was unconstitutional under the Supremacy Clause; (2) a permanent injunction against the assessment and collection of those taxes from federal contractors; and (3) an order requiring the refund of such taxes collected from federal contractors by the State of Washington and for which the United States had reimbursed its contractors.[1]

Declaratory judgment was sought on the grounds that the sales and use taxes as applied discriminated against the United States and its contractors and, alternatively, that the incidence of the taxes fell upon the United States itself. After the filing of an answer by the State (J.A. 9),

[1]The United States moved for the convening of a three-judge court pursuant to 28 U.S.C. § 2281. The statute was subsequently repealed for lawsuits filed after August 12, 1976, by Pub.L. 94-381, 90 Stat. 1119. Thereafter, by stipulation of the parties, with the approval of the trial court, the original proceeding was dismissed without prejudice and an identical action refiled for hearing before a single judge court. (R. 1, 5).

the United States moved for partial summary judgment (J.A. 14), requesting further proceedings only on the issue of the amount of taxes to be refunded. A cross-motion for summary judgment was filed by the State (J.A. 62).

The district court granted the motion of the United States for partial summary judgment, holding that the Washington statutes unconstitutionally discriminated against contractors for the federal government in violation of the Supremacy Clause. (J.S. App. C-1). The court held, however, that the legal incidence of the State's taxes fell on the private contractors and not upon the United States. The order of the court enjoined the further assessment and collection of the taxes, but by amended order the court modified its ruling to permit the State, pending appeal, to make protective assessments within the statute of limitations. (J.S. App. D-1).

The order of the district court was affirmed on appeal by the Court of Appeals for the Ninth Circuit but the appellate court declined to rule on the argument of the United States concerning taxable incidence. (J.S. App. A-15). A further appeal to this Court was taken and probable jurisdiction was noted on May 17, 1982. (J.A. 68).

II. RELEVANT FACTS

A. 1975 Amendments to Washington Sales and Use Tax Statutes.

Prior to the 1975 amendments to this State's sales and use tax law in issue on this appeal, the private or public owner of realty, or of an interest therein, was responsible for payment of state and local sales taxes on the value of building construction, measured by the total charges for labor, materials, other costs of construction, and profit. The Washington sales tax was a vendee tax payable by the consumer, which the vendor was required to collect and remit to the State. As a matter of state law the incidence of the tax was on the vendee; accordingly all federal construction was exempt from sales tax by reason

of the immunity of the United States. The sales and use tax system applied to construction both before and after 1975 was, and still remains, a part of the general tax system applicable to the purchase of other tangible personal property generally or the other acquisition of such property for the acquirer's own use.

In 1975, however, the increasing volume of construction by private contractors for the federal government led to efforts of the Washington State Legislature to include such activity within the State sales tax base.[2] The effect of the 1975 amendments was to place the sales tax on the cost of materials incorporated within federal construction projects by making the contractor the consumer or vendee for purposes of the tax.[3] For other construction projects, private and public, the incidence of the tax remained on the ultimate "consumer" or vendee of the project, measured not only by the cost of materials but by the labor component as well.[4]

The amendments to Washington sales and use tax statutes became effective July 1, 1975, but were expressly made inapplicable to federal construction contracts entered into prior to that date or subsequently executed after July 1, if the contract award had been made pursuant to a bid submitted before that date.[5] The general

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[2]Construction costs of approximately $1 billion were estimated for two projects alone, the Trident Nuclear Submarine base undertaken by the Department of the Navy and Bonneville Power House construction under the jurisdiction of the U.S. Corps of Engineers of the Department of the Army. (J.A. 19-20, 52).

[3]The 1975 amendments in fact encompass three separate enactments (1) Substitute House Bill No. 86 enacted as 1975 Wash. Laws ch. 90, § § 1, 2, 3, 4 (Br. App. A-1a); (2) § 5 of Substitute Senate Bill No. 2736 enacted as 1975 Wash. Law ch. 291, (Br. App. A-6a); and (3) House Bill No. 1229, enacted into law as 1975-76 Wash. Laws ch. 1, § § 1, 2, (Br. App. A-8a).

[4]By reason of earlier statutory amendments prior to 1975, public housing contractors and road contractors on local government and federal government projects are also treated as consumers or purchasers for purposes of the Washington sales tax.

[5]§ 4, 1975 Wash. Laws ch. 90, as amended by § 1, 1975-1976 Wash. Laws ch. 1.

conditions of the contracts involved in this appeal between the United States and its contractors provided for inclusion of applicable state and local taxes. With the adoption of the 1975 amendments to Washington's sales and use tax laws and in anticipation of litigation those general conditions were supplemented by a provision excluding sales and use taxes.[6] Under the change the United States agreed to reimburse its contractors for sales and use taxes paid to the state provided that such reimbursements would be refunded in the event the contractors should successfully challenge Washington's tax in litigation undertaken at the direction of the United States. Notwithstanding this provision, however, the United States subsequently took assignments of such refund claims from its contractors and brought this litigation in its own name. (J.A. 5).

B. Legislative Background to 1975 Amendments.

The changes in Washington sales and use tax structure in 1975 were the latest in a succession of amendments to the statutes for the taxation of building and road construction.

At the outset, when Washington's sales and use taxes were first enacted in 1935, all building contractors were treated in precisely the same manner. Sales of tangible personal property *to* the contractors were subject to the retail sales tax; and any use of such property by a contractor was subject to the use tax if it had not been first subjected to the sales tax.[7] There were no exceptions to this pattern; it applied to contractors with the federal and state governments, with local governments and with all

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[6]J.A. 31-32, 42-43.

[7]See 1935 Wash. Laws, chapter 180, § § 5(d), 31, and 32(c). It was unclear, however, whether the use tax would apply to a bailee's use of property, title to which remained in the bailor. The State Tax Commission's administrative position was that it would not. In 1959, the legislature explicitly provided that it would. See page 9, *infra*.

private parties, including non-profit or charitable entities. Indeed, this system applied to any tangible personal property purchased or otherwise acquired for the acquirer's own use, be that property food, an automobile, building supplies or anything else. And, as previously noted, the Washington sales tax was a vendee type of tax. For the vendor was required to collect the tax from the vendee and remit it to the State.[8]

In 1941, however, a major change occurred in the sales tax system as applied to contractors. The taxable transaction was no longer the sale *to* the contractor; rather, the taxable transaction became the sale *by* the contractor (including all of his services) to the property owner.[9] And the sale of property *to* the contractor became a non-taxable wholesale sale. This change had two important consequences.

First, the sales tax base was greatly expanded. Whereas before it had included only property sold to the contractor, it now included the total charge made by the contractor to the owner. And this charge, of course, included not just material costs, but labor costs and profit as well.[10]

Second, with respect to construction for the federal government, the tax base was, in contrast, severely diminished. Since the sales tax remained a vendee type tax, the transaction between the contractor and the federal government was immune from the tax—pursuant to the federal government's constitutional immunity—while most sales of property *to* the contractor were immune

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[8]1935 Wash. Laws, chapter 180, § 21.

[9]1941 Wash. Laws, chapter 178, § 2, amending § 5(d) of chapter 180, Laws of 1935. See, *Klickitat County v. Jenner*, 15 Wn2d 373, 130 P.2d 880 (1942).

[10]This 1941 expansion of the tax base to encompass the labor component had actually commenced in 1939 with respect to personal property. See 1939 Wash. Laws, ch. 225, § 2 which expanded the definition of "retail sale" to include the charges for improvements to personal property. The 1941 change enlarged this treatment to include the charges for improving real property as well.

because they were now wholesale sales rather than retail sales as before.[11]

Thereafter, as we have seen, the 1975 amendments here under attack by the United States essentially put federal contractors back in the same position they were in from 1935 through 1941, while leaving most other contractors subject to the 1941 change with two exceptions. In 1939, the legislature conferred a total immunity from state taxation upon public housing authorities with the result that their contractors, through the combined effect of the 1939 and 1941 changes, were in the same position as were federal contractors in 1941. Sales *to* these two types of contractors were in turn immune from the sales tax, as wholesale sales. Secondly, in 1943, contractors on public road projects were taken out of the scope of the 1941 amendments, and put back in the same position as they were in 1935.[12]

The following two additional changes should be mentioned to complete the pre-1975 picture:

(1) In 1959, the application of the use tax was extended by providing that tangible personal property acquired by or furnished to a contractor by means of a "bailment" would be subject to the use tax. See 1959 Wash. Laws, 1st Ex. Sess., ch. 3 § 10. This 1959 amendment, as applied to federal property used by a private party, was upheld by the Washington Supreme Court in *Boeing Company v. State*, 74 Wn.2d 82, 442 P.2d 970 (1968).

(2) And in 1971, public road construction, which in 1943 had been returned to the same status it had enjoyed from 1935 to 1941, was divided into two classes.[13] Road construction for the federal government and for all local

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[11]We say "most" at this point because the sales of property to a contractor remained retail sales if the property was not incorporated into the structure being built. Such sales would include principally construction equipment, ranging from hammers to bulldozers.

[12]See 1943 Wash. Laws, ch. 156, § 2.

[13]1971 Wash. Laws, 1st Ex. Sess., ch. 299, § § 3, 4.

governments remained the same as before; *i.e.*, the sales tax applied only on sales of materials and equipment. But construction of state public roads was now treated the same as any other construction for the state, *i.e.*, the sales tax applied to the total charges made by the contractor to the State, just as the 1941 amendments had first provided.

In sum, the system that existed prior to the 1975 amendments here under challenge encompassed three categories. First, with respect to construction for the United States and for a public housing authority, the sales and use taxes were imposed only on the contractor's equipment. Sales or use of materials to be incorporated by the contractor into the construction, and the charge made by the contractor for the construction itself, were exempt. Second, with respect to public road construction, for all governmental entities other than the State itself, sales or use taxes applied not only to the contractor's equipment but, as well, to materials to be incorporated into the construction. Third, with respect to all other construction—including road construction for the State—materials to be incorporated into the construction at the time of acquisition by the contractor were exempt, but the sales tax was applied to the total charge for the construction and thus encompassed the labor and profit components, as well as other costs, including materials.

The effect of the 1975 amendments can be very simply described in terms of these three categories. The first category was eliminated and construction for the federal government and public housing authorities was placed in the second, along with public road construction for entities other than the State. Construction in the third category—public road construction for the State and all other construction—remained taxed just as before.

C. The Respective Obligations of Buyers and Sellers to Pay the Tax.

As has been true since the sales tax was first enacted in 1935, the Washington sales tax is a vendee type of tax; *i.e.*, the legal incidence of the tax is upon the buyer. The

seller is required to add the tax to the sales price, collect it from the buyer, and then remit it to the State. Wash. Rev. Code § 82.08.050.[14]

If, however, the seller fails to collect the tax from the buyer the seller is still liable for payment of the tax to the State. *Ibid.* Further, in such a case the State has the option of enforcing the tax liability for this uncollected tax against either the seller or the buyer. *Ibid.* And should the State enforce the tax liability against the seller, the buyer remains indebted to the seller for the amount of tax, and the seller may proceed against the buyer to enforce that debt. *Ibid.*

Thus, the seller is always legally obligated to pay the tax to the State except in the case—relatively rare—in which the State proceeds directly against the buyer for collection. And, with this same exception, the buyer is always legally obligated to pay the tax to the seller.[15] But under the 1975 amendments, contractors with the federal government became retail *buyers* for sales tax purposes, whereas before they were retail sellers—albeit to a buyer that was constitutionally immune from taxation, the United States.

Two remaining points regarding Washington's sales and use tax system are to be noted. First, since 1935, Washington's sales and use tax system has been comprehensive in applying not only to construction projects but to the sale or acquisition of almost all tangible personal property, be it groceries, restaurant meals,

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[14]Quoted in full in J.S. App. H-4, 5.

[15]Normally, of course, the obligation of the buyer to the seller is discharged when the buyer pays the seller the purchase price, and the seller's obligation to the State is discharged later in time, when he makes payment to the State. But this is not always the case. In installment sales, for example, the seller must pay the State all the sales tax at the end of the reporting period in which the sale is made, even though the buyer makes payment of the tax to the seller later on, as part of the installment payments. See Wash. Admin. Code § 458-20-198. And, as pointed out above, where the seller has failed to collect from the buyer at all, and the State then proceeds against the seller, the seller may subsequently proceed against the buyer.

automobiles or furniture.[16] And second, local sales and use taxes are imposed by cities, counties and public transportation agencies on the same taxable events as the State tax but at lesser rates. Such taxes are administered and collected by the state on behalf of local governments, and accordingly are in issue here as well.

SUMMARY OF ARGUMENT

(1)

In determining whether the Supremacy Clause permits, or prohibits, a particular state tax upon those doing business with the Federal Government this Court has developed certain concepts or principles, all of which must be considered and applied in this case. One such principle is that the Supremacy Clause does not confer upon either the Government or those dealing with the Government a competitive advantage in the market place; nor does it unqualifiedly confer immunity upon the Government from the economic burden of a state tax. The second is the complement to the first: The tax may not threaten or impair a federal function. The third and fourth are ancillary to, and implement, the second: Persons doing business with Government may be taxed only if those "similarly situated" are similarly taxed; and the tax system must embody a political check upon the escalation of the tax.

In the instant case, we submit that the Court of Appeals misapplied the last three of these principles because it failed also to consider and apply the first.

(2)

In order to place the matter in proper focus let us first delineate the basic issue in this case, which arises from a very common factural pattern. Assume that A and B enter

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[16]The sales and use tax is Washington's major revenue source. In FY 1981 it brought in $1,165,247,000. Source: Washington State Department of Revenue, "1981 Tax Statistics," p. 6. Of this amount, approximately 15% was attributable to the entire construction industry.

into a business transaction. That transaction might involve a lease of property, with A as the lessor and B as the lessee; or a purchase of property, with A as the buyer and B as the seller; or, as here, a construction contract, with A again as the buyer and B as the seller—contractor.

Assume further that for administrative convenience, more effective collection procedures, or for other policy reasons, a State's tax system normally imposes its tax upon A rather than B. If, however, the tax cannot be imposed upon A because of an immunity, the system imposes the tax upon B instead (but only in those cases in which A is immune) in order to avoid the tax loss that would otherwise occur.

Is such a system unconstitutional when A is the federal government and B is the private party doing business with the federal government? More specifically does such a system violate the Supremacy Clause for the reason that it unconstitutionally discriminates against either the federal government (A) or the person with whom the Government is doing business (B)? Or, to frame the issue from the point of view of the State: Does the Supremacy Clause require the State to abandon its policy of taxing all A's, and instead to tax only B's, if it wishes to tax those B's who deal with the federal government?

We will show that in three previous cases, this Court has, in effect, answered these questions in the negative—refusing to apply the Supremacy Clause so inflexibly—and has sustained state taxing systems which made a change of the sort involved here. *United States v. City of Detroit*, 355 U.S. 466 (1958); *United States and Olin Mathieson Chemical Corp. v. Ill. Dept. of Revenue*, 202 F.Supp. 757 (N.D. Ill. 1962) aff'd per curiam, 371 U.S. 21 (1962); and *United States v. County of Fresno*, 429 U.S. 452 (1977). These three cases demonstrate that a change in taxable incidence of the sort involved in the instant case does not threaten any federal interest which the Supremacy Clause protects.

(3)

To show why this is so, we will examine the common

features of any tax system which changes the legal incidence of a tax from the Federal Government to the person with whom the Government is dealing. To begin with, we note that if such a change is not allowed, the Government's immunity takes on much more than just "symbolic importance." *United States v. New Mexico*, 102 S.Ct. 1373, 1383 (1982). The immunity will take on economic importance as well. For the Government will have a competitive advantage in the marketplace enjoyed by no other parties. We will illustrate, through various examples, precisely how this competitive advantage would arise, and also how it would be eliminated by a switch in the incidence of the tax.

These illustrations will also show, however, that any such switch provides a strong, perhaps irresistible, incentive for the Government to relinquish all of the economic benefit which would otherwise stem from its tax immunity. For if it does not, it will run the risk of finding few, if any, persons willing to do business with it. And it is precisely at this point that the constitutional problem arises. For if the Government decides not to relinquish the economic benefit stemming from its tax immunity, it will have effectively "shot itself in the foot," by reducing—perhaps even to zero—the number of persons who would be willing to do business with it.

Believing that the Supremacy Clause spares the Government from this choice, and even from the consequences of such a self-inflicted wound, the Court of Appeals invalidated the Washington tax system. What the court failed to recognize, however, is that *any* tax system which makes a switch in taxable incidence inevitably puts the Government to just such a choice.

(4)

To show that this is so, we will examine the tax systems challenged in *Detroit*, *Olin Mathieson*, and *Fresno*. By shifting the incidence of the tax, those tax systems required the Government either to forego the economic advantage stemming from its tax immunity, or

to place the person with whom it was dealing at a competitive disadvantage. But the tax systems in each case were nevertheless upheld. Why? Because, we submit, the Supremacy Clause does not protect the Government from the choice—or perhaps more accurately, dilemma—which so concerned the Court of Appeals. Rather, as shown by *Detroit, Olin Mathieson, Fresno,* and also by *U.S. v. New Mexico,* 102 S.Ct. 1373 (1982), the protection it affords is much more narrow and modest.

What the Supremacy Clause does do is to assure the Government that as a buyer (other factors being equal) the tax system—as applied to those with whom it deals—cannot make the total cost of its purchases higher than for nonfederal buyers. Similarly, if the government is a seller, the tax system cannot make the economic benefit realized by the Government less than it would be for nonfederal sellers. But the Supremacy Clause does not further assure, as the Court of Appeals mistakenly concluded, that the Government's costs will be lower or that its realized economic benefit will be higher. And this is the essence of what we will hereafter refer to as the "no competitive disadvantage" principle.

(5)

Not only the results but the rationales in *Detroit* and *Fresno* require this principle of "no competitive disadvantage."[17] Under *Detroit,* the function of the Supremacy Clause is not to preserve for those dealing with the Government any "economic preference over their neighboring competitors * * *" *Detroit,* 355 U.S. at 474. And under *Fresno,* which focuses on the other party to the transaction (namely, the Government), the function of the Supremacy Clause is not to preserve, even for the Government itself, any tax preferences or the competitive advantages stemming therefrom. In turn, under *Detroit* and *Fresno* together, *neither* party is constitutionally entitled to these benefits. Yet the Court of Appeals'

[17]*Olin Mathieson,* of course, was a per curiam affirmance, without opinion.

decision in the instant case assures a loss in state taxes which inevitably confers such economic benefits on one or the other.

Fresno is the most important of our trilogy of cases because it focuses upon the nature of the Government's interest which the Supremacy Clause protects and the means by which that interest is to be protected. The Supremacy Clause assures that federal functions will not be impaired. And this assurance is provided by application of the political check doctrine, which owes its origin to the landmark case of *M'Culloch v. Maryland,* 17 U.S. (4 Wheat.) 316 (1819). Under that doctrine, a State may not single out the Government for economic burdens not shared by a reasonably large constituency which is similarly situated and similarly burdened. The Government, in short, cannot be made *worse* off than this constituency. It has, however, no right to be better off. And we will show that Washington's sales and use tax system, which is the broad-based mainstay of its entire revenue system, provides at least as broad a political check as was provided in *Fresno,* and thus removes any risk of impairment of a federal function.

Fresno also places in perspective the familiar principle that a state may tax those dealing with the Government only if it equally taxes those similarly situated. Although expressed in terms of protecting those who deal with the Government, this principle is derived from and, most importantly, must take its substance from the protection which the Supremacy Clause affords the Government itself. The Supremacy Clause, after all, is not simply an alter ego of the Equal Protection Clause.

As a matter of statutory mechanics, federal contractors under Washington law are undeniably treated differently from most other contractors. The critical question, however, must always be that focused upon in *Fresno*: What is the impact of that difference in mechanics on the Government itself? We will show that, far from placing the Government at a disadvantage, the Washington tax system actually preserves an advantage of

the Government—which, unlike other purchasers of construction work, is free from the burden of a tax on its contractors' labor or services.

The "no competitive disadvantage" principle which we here advocate also eliminates a difficulty in this area which has been noted many times by the Court; *i.e.*, the problem of having to ascertain in any given case who actually bears the economic burden of a particular tax. No such difficulty would arise under the approach proposed here; for that approach provides a litmus test which is available from the face of the statute itself. It requires only an understanding of the whole statutory scheme, and not the often conflicting evidence from economic experts.

It does, however, rest upon the assumption that similar market forces in both the private and public sectors will have similar results and that, accordingly, the economic burden of a tax will be allocated in a similar manner, despite any difference in legal incidence. This assumption must underlie as well any logical application of both the "similarly situated" standard and the political check doctrine, *viz* an application which does not afford the Government, or those dealing with it, a competitive advantage in the marketplace.

(6)

Lastly, we will show that approach we propose follows that taken by this Court in two other areas in which state taxes have been challenged and to which this Court has looked for guidance in resolving discrimination issues arising under the Supremacy Clause. Those two areas are taxation of national banks, under 12 U.S.C. § 548, and its predecessor Rev. Stat. § 5219, and taxation of transactions or property involving interstate commerce.

In both of these areas, the Court has rejected standards based on mechanical similarities and has instead looked to the operative effect of the tax system as a whole. It has thereby fully protected the federal interest involved, while preserving to the States flexibility in fashioning their tax systems. We ask for nothing more here.

ARGUMENT

I. Introduction: The Basic Issue

The general guidelines governing state taxation of transactions in which the federal government is involved are summarized in the Court's latest opinion in this field:

> "* * * tax immunity is appropriate in only one circumstance: when the levy falls on the United States itself, or on an agency or instrumentality so closely connected to the Government that the two cannot realistically be viewed as separate entities. * * *" *United States v. New Mexico,* 102 S.Ct. at 1382.

As further stated in that opinion:

> "With the abandonment of the notion that the economic—as opposed to the legal—incidence of the tax is relevant, it becomes difficult to maintain that federal tax immunity is designed to insulate federal operations from the effects of state taxation. *It remains true, of course, that state taxes on contractors are constitutionally invalid if they discriminate against the Federal Government, or substantially interfere with its activities.* See *United States v. County of Fresno,* 429 U.S. 452, 463 n. 11, 464 (1977); *Moses Lake Homes, Inc. v. Grant County,* 365 U.S. 744 (1961); *City of Detroit v. Murray Corp.,* 355 U.S. 489, 495 (1958). * * *" 102 S.Ct. at 1383, n. 11. (Emphasis supplied)

These guidelines provide two important starting points for our analysis.

First, the fact that the tax may ultimately be paid from the federal government's pocket does not, in and of itself, mean that it discriminates against the Government, interferes with its activities, or impedes a federal function. This is true even if the economic burden upon the federal government is just as heavy as it would be if the legal incidence of the tax as well fell upon the Government. Some other factor must also be present before such discrimination or interference is found. A logical candidate for such a factor would be of course, a *lighter* tax burden being imposed upon someone else in a position similar to that of the Government.

The second point is closely related to the first. The protection which the Supremacy Clause affords those persons dealing with the Government is only derivative. By this we mean that the test for determining whether a tax is discriminatory, if its legal incidence is imposed upon such persons, must be derived from the effect of that tax upon the Government itself. After all the purpose of the Supremacy Clause is only to protect federal interests—not those of private parties.

But what is the precise test of discrimination against the federal government, or substantial interference with its activities, when a state makes a shift in the legal incidence of a tax such as that involved here? That was the central issue in *United States v. County of Fresno*, 429 U.S. 452 (1977), in *United States v. City of Detroit*, 355 U.S. 466 (1958), and in *United States and Olin Mathieson Chemical Corp. v. Ill. Dept. of Revenue*, 202 F.Supp. 757 (N.D. Ill. 1962) aff'd per curiam 371 U.S. 21 (1962). And it is the central issue here.

This issue is most readily understood, we believe, by placing it in the broad context of a state's tax policy. A State may decide as a matter of tax policy to place the legal incidence of a tax upon one party to a transaction rather than the other for a variety of reasons. If a lease of real property is involved, for example, a State may decide to tax the lessor-owner rather than the lessee simply for administrative convenience. The system for taxing all other real property owners does not have to be changed at all in order to fit the owner who is also a lessor. Further, the prospects for collection are enhanced through a lien upon the entire fee interest, rather than upon a leasehold interest alone.

Similarly, if a sales or use tax is involved, a State may place the legal incidence on the buyer instead of the seller for any number of reasons.[18]

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[18]There is no single national pattern in this regard. See, J. Due, State and Local Sales Taxation: Structure and Administration, Public Administration Service (1971) 25-26. As Professor Due points out, there are sound policy reasons for either a vendor type of tax or a consumer type of tax, to use his terminology. Due, *Ibid.*, 26-28.

There will, however, be certain cases in which adhering to this normal pattern of imposing the tax on the lessor or buyer would result in no tax at all. These would be cases in which, for one reason or another, the lessor or buyer is immune. A state statute or constitutional provision may exempt charitable organizations, municipal corporations, or political subdivisions.[19] Or, as here, the immunity may arise from the Federal Constitution itself.

Whatever the reason for the immunity, the State is confronted with two alternatives in such a case. It can either forego the tax altogether; or it can switch the legal incidence of the tax from the immune to the non-immune party.

Certain consequences, which are critical to our analysis, flow from each alternative. If the State foregoes the tax, the State's loss will inevitably be someone else's gain. Exactly how that gain might be divided up between the two parties will, of course, depend upon the relative bargaining power and skill of each. And the relative bargaining power of each may well depend on market conditions. What is certain, however, is that in any such case the exempt party, such as the Government, has a competitive advantage over its non-exempt counterpart, no matter what the market conditions might be.

As a lessor, the Government can offer a lower rent to a prospective lessee while still receiving a higher net return than its taxable counterpart can receive. Assume, for example, that the market composed of private lessors and lessees establishes an annual rental value of $11,000 for a particular parcel of realty. Assume further that from the $11,000 the private lessor would have to pay $1000 in property taxes for an after-tax return of $10,000.

If, however, that lessor is the Government or another exempt entity, the lessor has a $1000 advantage. The lessor could share some of this advantage with its lessee by offering a lower rent—*e.g.*, $10,750, and still have a return

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[19] *Cf.*, for example, the types of state exemptions provided by California law as discussed in *Fresno* and by Michigan law, as discussed in *Detroit*.

$750 higher than that received by the non-exempt lessor.

So too as a buyer, the Government can offer a higher price to a prospective seller, but still incur a lower total cost than its taxable counterpart would incur. Assume, for example, that the total cost of an item in a sales transaction between private parties is $10,600—consisting of a $10,000 sales price and $600 of sales tax to be paid by the buyer. But if the buyer is the Government or some other exempt entity, the buyer has a $600 advantage, which would allow it to pay a higher price, say $10,500, but still have a total cost $100 less than that of the non-exempt buyer.

If, however, the State switches the legal incidence of the tax, this competitive advantage is eliminated, along with the State's tax loss. The potential impact on each of the parties should also be noted. If the Government is willing to bear the *economic* burden of the tax, the other party, on whom the tax is now legally imposed, is not really affected economically at all. To use our lease example: The Government would receive $10,000 in rent—the same as the after tax return to the private lessor; and the lessee would additionally pay $1000 in tax, for a total cost of $11,000—the same as for other lessees of identical property.

If the Government, however, attempts to keep the economic benefit of its tax exemption, *i.e.*, if it attempts to obtain $11,000 in rent, the lessee will bear not only the legal incidence of the tax but the economic burden as well. His total cost would be $12,000. And this prospect could well cause him to decide not to do business with the Government at all and to rent, instead, from a private lessor, for a total cost of only $11,000. Collectively, the number of lessees willing to lease from the Government would be reduced perhaps to zero.

Similarly, to use our sales example: If the Government decides that it is only going to pay $10,000, rather than $10,600, the prospective seller would have a net return of only $9,400, rather than the $10,000 he would realize from a similar transaction with a private party.

Under these circumstances, the number of sellers willing to do business with the Government would be reduced, again perhaps to zero.

It is this type of potential discrimination against those dealing with the federal government which prompted the Court of Appeals to strike down Washington's sales and use tax as applied to federal contractors. More broadly, the court held that the Government cannot be put in a position which requires it to give up the economic benefit of its tax exemption in order to avoid putting those who would deal with the Government at a competitive disadvantage. (J.S. A-11 to A-14)

Contrast this situation, in which there is only a shift in the legal incidence of the tax from the Government to the Government's lessee or seller, with a situation in which the State does something more. To take the most obvious example, the State might also increase the rate of the tax. To use our lease illustration, the State might increase the property tax rate so that the tax on the Government's lessee is $1,100, rather than just $1,000. And with our sales illustration, the State might increase the rate from 6 to 7 percent, so that the tax will be $700 rather than $600.

In both of these illustrations, the Government cannot remove the competitive disadvantage of its lessee or seller by simply giving up the economic benefit of its own immunity. The lessee or seller would still be economically disadvantaged to the extent of $100. And conversely, if the Government did remove this competitive disadvantage, by reducing the rent or increasing the compensation to its seller by this extra $100, then the Government itself would be directly disadvantaged. It would be receiving $100 less in rent, or paying $100 more in costs than other lessors or buyers. Such an increase in the tax rate, in short, does more than remove the competitive advantage stemming from the Government's tax immunity. It affirmatively creates a competitive disadvantage and either directly or indirectly makes the Government worse off than other lessors or buyers.

It is this second type of situation, we submit, but not the first, which the Supremacy Clause forbids. The Government has no right to be economically better off than other lessors and buyers. But it does have a right to be no worse off.

As we shall show, the taxing systems involved in *Detroit, Olin Mathieson,* and *Fresno* placed the Government in this first situation, though not in the second. And this is why those taxing systems were upheld.

II. Detroit, Olin Mathieson and Fresno All Upheld Taxing Systems Which Involved Shifts in the Legal Incidence of a Tax Conceptually Indistinguishable from the Shift Involved Here and Which Presented by Reason of that Shift the Same Potential Consequences to the Government and Those with Whom it Deals as are Presented Here.

A. Detroit

At issue in *Detroit* was the validity of a Michigan statute which imposed upon lessees of tax-exempt property a tax equal to that which would be paid were the property not exempt. The Government challenged the tax as applied to the Borg-Warner Corporation, a private firm leasing Government property for use in its manufacturing business.

The lease agreement between the Government and Borg-Warner provided that Borg-Warner could deduct from the rental any taxes paid by it under the Michigan statute. 355 U.S. at 468. The economic burden of the tax was thus effectively shifted to the Government. But observe the consequence if this shift had not taken place and if the Government had attempted to keep the economic benefit of its tax immunity: Borg-Warner would have been at a disadvantage as compared with lessees from taxable lessors. The Michigan statute thus had the effect of forcing the Government to reduce the rent by the amount of the tax if Borg-Warner was not to be put to this disadvantage. This possible disadvantage, which might have been characterized as a type of potential

discrimination, was inherent in the application of the statute. Nevertheless, the Court upheld it.

B. Olin Mathieson

At issue in *Olin Mathieson* was the validity of the Illinois retailers occupation tax as applied to sales of aircraft engine starter cartridges by Olin Mathieson to the U.S. Air Force. (202 F.Supp. at 761). By its terms, this tax was imposed only upon the seller. But Illinois law also imposed upon the *purchaser* the traditional type of use tax, equal in amount to the retailer's occupation tax. And the seller was required to collect that use tax from the buyer.

In order to prevent both taxes from applying to the same transaction, the retailer who paid the occupation tax to the state was allowed to keep the use tax which he had collected from the buyer. Technically, then, both the retailer dealing with the Government and the retailer dealing with a non-federal purchaser were subject to the same retailers occupation tax. The legal incidence was switched, however, through the mechanism of the use tax. When the retailer collected the use tax from the non-federal purchaser, he just pocketed it. And the result would be precisely the same as if the retailer paid no occupation tax at all, but simply remitted the use tax to the state. The incidence of the tax was upon the non-federal purchaser because he was legally required, through the use tax, to reimburse the retailer for his occupation tax.

The Government's challenge to the retailers occupation tax, as applied to a retailer selling to the Government, focused on this reimbursement feature.

> " 'The tax which the federal government has here assumed by contract is the tax obligation due the State of Illinois from Olin Mathieson, the retailer. Plaintiffs' argument on discrimination concedes that the use tax is not exacted from the federal government and it is urged by plaintiffs that a retailer who sells to the federal government must pay the occupation tax out of his own pocket because he

cannot collect the use tax from the purchasing sovereign; whereas a retailer dealing with a purchaser who is not the federal government need not pay the occupation tax when he collects the use tax from such purchaser.'" 202 F.Supp. at 760.

The Government again was put to an unpalatable choice: Either it reimbursed the seller, Olin Mathieson, for the retailers occupation tax, and thereby lost the economic benefit of its own immunity, or it placed Olin Mathieson at a competitive disadvantage. Nevertheless the court upheld the tax in a per curiam affirmance.[20]

C. Fresno

The California statute involved in *Fresno* was similar to the Michigan statute involved in *Detroit*. It authorized counties to impose a property tax upon possessory interests in improvements on tax-exempt land.[21]

The Government challenged the California tax as applied to possessory interests of U.S. Forest Service employees living in federally-owned housing supplied to them as part of their compensation. The rent paid by the employees was deducted from their paychecks, and was based upon the fair rental value of similar housing in the private sector, which presumably included the private lessors' costs for property taxes.

In effect, the Government was acting in *Fresno* in two separate capacities; first, as lessor of real property and second as a buyer of services, *i.e.*, the services of the Forest Service employees.

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[20]In contrast with the statutes challenged in *Detroit*, *Fresno* and here, the statute challenged in *Olin Mathieson* probably did not represent a conscious legislative effort to shift the legal incidence of the tax in order to plug what was perceived as a loop-hole in transactions involving exempt entities. For the retailers occupation tax was adopted in Illinois in 1933, well before the use tax was adopted in 1955. (CCH Ill. State Tax Reporter, 6071). Nevertheless, the operative effect of the combination was to shift the incidence of the tax from the exempt purchaser to the non-exempt seller.

[21]It differed from the Michigan statute, however, in that the measure of the tax was not the full value of the property but rather the value of only the possessory interest.

As a lessor, the Government was placed in the same position as it was as lessor in *Detroit*. If it did not reimburse its lessees for the tax, and thereby give up the economic benefit of its own tax immunity, it placed those lessees at an economic disadvantage. As a buyer of services, the Government was placed in the same position as it was in *Olin Mathieson*: If it did not reimburse its employees for the tax, by deducting less from their paychecks, its employees would be presumably receiving less in compensation than they could obtain in the private sector, and thereby be discouraged from working for the Government.

In *Detroit* and *Olin Mathieson*, the Government had agreed by contract to make reimbursement for the tax. In *Fresno*, however, it had not. Nevertheless the Court upheld the tax.

III. The Rationale of Detroit and Fresno Require That the Shift in Legal Incidence Involved Here be Upheld.

A. The Rationale of Detroit

In rejecting the Government's assertion that the Michigan statute involved in *Detroit* was discriminatory, the Court stated:

> "As suggested before the legislature apparently was trying to equate the tax burden imposed on private enterprise using exempt property with that carried by similar businesses using taxed property. Those using exempt property are required to pay no greater tax than that placed on private owners or passed on by them to their business lessees. In the absence of such equalization the lessees of tax-exempt property might well be given a distinct economic preference over their neighboring competitors, as well as escaping their fair share of local tax responsibility. * * *" 355 U.S. 466, 473-474.

Under this rationale, it is not the function of the Supremacy Clause to preserve economic preferences for those who deal with the federal government, and thereby

allow such entities to escape their fair share of tax responsibility.

As noted by the Court, either the lessor or the lessee would bear the economic burden of the tax if the lease were between non-exempt parties. And apparently it mattered not on which party the economic burden actually fell, *i.e.*, whether it was passed on to the lessee or not. In either case, the City of Detroit would receive its tax. And it was only fair that the city should likewise receive its tax even if the lessor was tax exempt.

Further, while lessees of tax exempt property "might well be given a distinct economic preference over their neighboring competitors" if the tax on them were invalidated, the use of the phrase "might well" shows the Court to be alert to the possibility that they might not. This would be the case, of course, if the Government were charging its lessee full rental value, with no offset for the tax. In that event, the economic preference would flow to the Government, not the lessee.[22]

As *Fresno* shows, however, the Supremacy Clause does not provide such an economic preference for the Government itself any more than it provides a preference for those who deal with the Government.

B. The Rationale of Fresno

The Court in *Fresno* explicitly recognized that the Government possessed, by reason of its tax immunity, a competitive advantage, and that the Supremacy Clause did not prohibit a state from taking that advantage away. The Court's opinion says:

> "The tax threatens to interfere with federal laws relating to the functions of the Forest Service *only* insofar as it may impose an economic burden on the Forest Service—causing it to reimburse its employees

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[22]As already observed, the lease agreement between the Government and Borg-Warner actually provided that the tax, if upheld, would be taken out of the rental payment. This would indicate that the economic preference would probably flow to the Government, not to Borg-Warner, if the tax were struck down.

for the taxes legally owed by them or, failing reimbursement, removing an advantage otherwise enjoyed by the Federal Government in the employment market. There is no other respect in which the tax involved in this case threatens to obstruct or burden a federal function." 429 U.S. at 464. (Emphasis in original).

And most importantly, footnote 12 states:

"The Federal Government would otherwise have had the power—enjoyed by no other employer—of giving its employees housing on which no property tax is paid by them either directly or indirectly as rent paid to a landlord who himself paid a property tax."

The choice to which the Government was put, as thus described by the Court, was not the only choice involved, however. If the Government attempted to keep the economic benefit of its immunity, instead of sharing it with its employees by charging them less than full rental value, the addition of the tax would result in those employees incurring housing costs *greater* than other lessees. The Government, then, would be put to the choice of either reimbursing its employees for the tax or, failing such reimbursement, actually leaving them in this worse position.[23]

How the Government made this choice, after it found out from this Court that the California tax was valid, is not known. And in any event it is irrelevant. For under *Fresno*, it is clear that the Supremacy Clause does not invalidate a state tax system, such as California's, which puts the

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[23]Thus, Justice Stevens was certainly correct in suggesting, in his dissent, that the employees would be worse off than other tenants if the Government were to continue to charge full rental value, which includes a property tax component. See 429 U.S. at 469. The answer to Justice Stevens' point, however, is that the Supremacy Clause has never vested in the Government a type of "right of first refusal." The right of a state to tax one dealing with the Government has never depended on the Government's decision to actually reimburse that person for the state tax. And this is the reason that we do not base our argument upon the fact that the Government in this case has actually agreed to reimbursement the contractors subject to the Washington tax for the amount of that tax. (J.A. 31-32, 42-43)

Government to that choice. This becomes even clearer as we further examine the rationale of *Fresno*, especially its further development and application of the "political check" doctrine.

The starting point for the Court in *Fresno* was an analysis of *M'Culloch v. Maryland*, 17 U.S. (4 Wheat.) 316.

> "The Government relies principally on the landmark case of M'Culloch v. Maryland. There the State of Maryland imposed a tax on notes issued by 'any Bank * * * established without authority from the State.' The only such bank in Maryland was the Bank of the United States, created and incorporated by Act of Congress in order to carry out Congress' enumerated powers. No similar tax was imposed on the issuance of notes by any other bank in Maryland. The Court held the tax to violate that part of the Federal Constitution which declares that the laws of the United States are the 'supreme law of the land.' An Act of Congress had created the bank in order to carry out functions of the National Government enumerated in the United States Constitution. The Court noted that the power to tax the bank 'by the States may be exercised so as to destroy it,' 4 Wheat, at 427 * * * and consequently that the power to tax, if admitted, could be exercised so as effectively to repeal the Act of Congress which created the bank. If the State's power to tax the bank were recognized in principle, the Court doubted the ability of federal courts to review each exercise of such power to determine whether the tax would or would not destroy a federal function. Finally, the Court rejected the State's argument that the power to tax involves the power to destroy only where the taxing power is abused, and that the Court should simply trust the States not to abuse their power to tax a federal function just as it must trust a State not to abuse its power to tax its own citizens. *The Court rejected the argument because the political check against abuse of the power to tax a State's constituents is absent when the State taxes only a federal function. A State's constituents can be relied on to vote out of office any legislature that imposes an abusively high tax on them. They cannot be relied upon to be*

similarly motivated when the tax is instead solely on a federal function. (Emphasis supplied) 429 U.S. 457-459.

Several points should be noted here. Whatever the precise test for a discriminatory tax might be, the purpose of such a test is to prevent the impairment of a *federal function,* and not simply to protect, as such, those dealing with the Government. Any protection afforded those dealing with the Government is solely derivative and secondary. The scope and content of that protection must be derived from the scope of the protection which the Supremacy Clause affords to the Government itself.[24]

Moreover, the protection which the Supremacy Clause affords to the Government itself does not prevent the imposition of an economic burden, stemming from the state tax, upon a federal function. See, *Fresno,* 429 U.S. 452, 460. There must, however, be a political check so that this economic burden cannot be escalated without a similar burden on a broad constituency being escalated as well. An abusive level of taxation is thereby prevented through the political process, and there would be no danger of impairment of a federal function. This point is emphasized again in footnote 11:

> "A tax on the income of federal employees, or a tax on the possessory interest of federal employees in Government houses, if imposed only on them, could be escalated by a State so as to destroy the federal function performed by them either by making the Federal Government unable to hire anyone or by causing the Federal Government to pay prohibitively high salaries. This danger would never arise, however, if the tax is also imposed on the income and property interests of all other residents and voters of the State." 429 U.S. 452, 463.

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[24]Thus, in *United States v. New Mexico,* 102 S.Ct. at 1383, n. 11, the Court said: "It remains true, of course, that state taxes on contractors are constitutionally invalid if they discriminate against the Federal Government or substantially interfere with its activities."

The Court's focus is upon the effect of the tax upon the Government itself. No mention is made of discrimination against the contractors, as such; and properly so.

The Supremacy Clause, in short, does not protect federal functions from the economic burden of a tax which makes the performance of that function just as costly as it would be if performed by someone else. It does not, in other words, guarantee that the Government can perform a function more cheaply than anyone else. Rather, it protects federal functions from burdens which make the performance of that function *more* costly. *And that is all it does.*

This, of course, is but another way of saying that the Supremacy Clause does not preserve to Government the economic benefit of its own tax immunity.[25] It does not assure the Government that it will be better off, but only that it will be no worse off, than others performing a similar function. This, we submit, is the essence of the test for unconstitutional discrimination as established in *Fresno*.

A final comment before leaving *Fresno*. What class of persons was it that provided the political check in *Fresno*? Although it is clear that such a check existed—otherwise the California tax would not have been upheld—it is less clear precisely who provided it.

The class certainly encompassed more than just those other lessees, renting from other tax-exempt lessors, who were also subject to the same California possessory interest tax as were the Forest Service lessees. Did the rest of the class, however, consist of lessees from private taxable lessors? Or did it consist of the taxable lessors themselves?

Arguably, it was the lessees of these taxable lessors. As the Court observed:

> "With respect to non-tax-exempt land, California imposes a property tax on the owner. No tax is imposed directly on a renter of non-tax-exempt land. However, the tax on the owner is presumably reflected in the rent and the renter may thus pay the tax indirectly." 429 U.S. 452, 455, n. 3.

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[25]As the Court put it in *United States v. New Mexico*, that immunity is now largely "symbolic." 102 S.Ct. at 1382.

If all lessees of taxable real property were in fact paying the tax indirectly, because it was reflected in the rent, then it was the lessees who composed the class. For they would have incurred the economic burden of the tax.

But it is not at all difficult to conceive of instances in which the presumption that all lessees paid the tax indirectly might well be wrong. For example, lessors could easily face, in a recessionary economy, a "buyers' market" in which they could not pass on tax increases to their tenants in the form of higher rent. Indeed, in such an economy, lessors might even be forced to lower rents, even though taxes are not lowered, but might even be increased.

Surely, after *Fresno,* the California tax would not be invalidated by showing that this presumption was wrong. The validity of that tax should not depend upon the uncertainties of economic evidence, any more than it should depend upon whether or not the Government makes reimbursement for that tax. *Cf., Fresno,* 429 U.S. at 464 and p. 27, *supra.*

What we do know for certain, however, is that *someone* bears the economic burden of the tax. Normally the presumption made in *Fresno* would be correct; the lessees would bear the burden. But in some circumstances it might be the lessors who bear the burden; and in others, the burden might actually be spread among both. The critical point is that whatever the circumstances, there will inevitably be a large group of persons whose economic interests are affected by the tax. That group will provide the political check; and it is unnecessary to know, from economic experts or from anyone else, precisely who is in that group at any time.

Similar considerations should apply, we submit, in applying the familiar "similarly situated" test. The close relationship between that test and the political check doctrine is shown by the following passage from *Fresno*:

> "The rule to be derived from the Court's more recent decisions, then, is that the economic burden on a federal function of a state tax imposed on those who deal with the Federal Government does not render

> the tax unconstitutional so long as the tax is imposed equally on the other similarly situated constituents of the State. [Footnote omitted.] This rule returns to the original intent of M'Culloch v Maryland. The political check against abuse of the taxing power found lacking in M'Culloch, where the tax was imposed solely on the Bank of the United States, is present where the State imposes a nondiscriminatory tax only on its constituents or their artificially owned entities. * * *" 429 U.S. at 462, 463.

By reason of the presumption that lessees from taxable lessors actually incurred the economic burden of the lessor's tax, those lessees could be viewed as the "similarly situated constituents of the State." But again, what if that presumption is wrong? Would the "similarly situated" test then require that the tax be struck down?

Like the similar question we have raised in the context of the political check doctrine, the Court did not address this question; but surely the answer must also be "No." After all, if lessees from private lessors have the ability, in a "buyers' market," to make the lessor bear the economic burden of the tax, there is no reason to assume that their counterparts, lessees from the Government, would have any less ability to make the Government bear the economic burden of *their* tax. Conversely, if private lessors have the ability to make their lessees bear the economic burden of the tax on the lessors, so too the Government would surely have the power to make its lessees bear the economic burden of the tax on them. In either case, both groups of lessees are similarly taxed—or not taxed. The similarly situated test, in short, presents a problem only if one assumes that market forces work one way in the private sector but another way when the Government is involved. A state's taxing power should not be struck down, under the guise of applying the "similarly situated" test, on the basis of such an untenable and unreasonable assumption.[26]

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[26]The "similarly situated" test, if it is applied mechanically, and independently of the political check doctrine, will inevitably produce some unsolvable conundrums. The test cannot mean that those

To summarize our discussion of *Fresno*: The test for discrimination developed and applied in *Fresno* does not preserve for the Government the economic benefit of the Government's tax immunity. It does not assure the Government that its costs in performing a function will be any less than the costs incurred by others performing similar functions. Rather, through the political check doctrine, it assures the Government that all other factors being equal the Government's cost in performing that function cannot be one penny *higher* by reason of the State's taxing system. But it assures the Government no more.

The application of this test does not require that a Court determine who actually bears the economic burden of a tax, either in the private sector or in a transaction in which the Government is involved. Nor does it require identification of who specifically provides the necessary political check under various economic circumstances. It only requires that a meaningful political check actually exists, under any and all economic circumstances.

And, as we shall next show, Washington's system for taxing federal contractors meets this test.

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similarly situated to those dealing with the Government must be subject to the same identical tax, with the same legal incidence upon those dealing with the Government and those similarly situated. For in *Detroit, Olin Mathieson, Fresno,* and this case, the legal incidence of the tax was switched, and, by hypothesis, those similarly situated are not similarly taxed. Accordingly, to make sense, the test must take into account the *economic* incidence of the tax. With the exception, however, of a cost-plus contract, it is difficult and perhaps impossible to determine the extent to which the economic incidence or burden of a tax falls on one party or the other. Indeed in *Detroit,* the Court pointed out that the Government, in its brief in *Alabama v. King & Boozer,* 314 U.S. 1 (1941), described the economic burden test as "illusory and incapable of consistent application." *Detroit,* 355 U.S. 466, 473, n. 4. *Cf., Graves v. New York,* 306 U.S. 484-485 (1939).

The problem disappears, however, if one makes the only assumption that is really logical: That despite the difference in legal incidence of the taxes, similar economic conditions in the marketplace will distribute the economic burden of the taxes in a similar manner. Under this assumption, those similarly situated will be similarly taxed—or not taxed. And it becomes unnecessary to answer the often unanswerable question: Which party to the transaction actually bears the economic burden of the tax?

IV. Washington's Taxing System is Valid Under the Test for Discrimination Established in Fresno, and Possesses the Necessary Political Check.

For purposes of this discussion, we put to one side the fact that contractors with the Government are taxed in a manner identical to that by which two other groups of contractors are taxed; *i.e.*, contractors with public housing authorities and builders of public roads for all government bodies except the State. Under our submission, there is no discrimination against contractors with the Government, as compared with each and every other contractor doing business with all other persons or entities, without exception.[27]

A brief recapitulation of the differences between the treatment of the two categories of contractors may be helpful. There is no difference, of course, in the tax rate. The base to which that rate is applied, however, is different. The base in the first category, which includes federal contractors, encompasses only the cost or value of materials: The base in the second category encompasses the total contract price, including labor charges and any profit. And most importantly, the incidence of the tax is different: The legal incidence of the tax falls upon contractors in the first category, while it does not fall upon contractors in the second. This is so because contractors in the second category have a statutory right to reimbursement from their customers. See, p. 9, *supra*.

The state, then, will always receive less revenue—all other factors being equal—from construction projects in the first category, including federal projects—than it will from similar projects in the second. And this means that the total cost to the customer—such as the United States—will necessarily be less, even if the customer fully reimburses the contractor for the tax on materials. Thus,

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[27]Thus, there is in this case no issue as to the adequacy of the size and composition of the class, such as concerned Justice Stevens in his dissent in *Fresno*, 429 U.S. 471, 472, and Justice White in his dissent in *Montana v. United States*, 440 U.S. at 168, 170 (1979).

with full reimbursement, the cost of performing the federal function is necessarily less than that which would be incurred by a customer in the second category. And all that *Fresno* requires is that the cost of performing that function be no greater, by reason of a state's tax system, not that it actually be less.

Admittedly, Washington's system puts the Government to an unpalatable choice: If it does not reimburse and attempts to keep the economic benefit of its immunity, it runs the risk of finding few, if any, contractors willing to do business with it. But that is no different from the choice which the Government faced in *Detroit, Olin Mathieson,* and *Fresno.*[28]

Who, then, provides the necessary political check under Washington's system? If the economic burden of the tax on construction in the second category falls upon the customers, then it is these customers as a class that provide the check. If it falls upon the contractors, because of these customers' superior bargaining power, then the contractors provide the check. And if the economic burden is split, both the contractors and the customers provide the check together.

Nor should it be overlooked that the tax here involved is Washington's general sales and use tax. It is the same tax as is imposed upon almost all retail sales of tangible personal property, and on a wide variety of

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[28]Contractors in the first category, such as federal contractors, may have to part with their money before contractors in the second do so. For they must normally pay the tax to the seller of the materials at the time of sale, and they may not be reimbursed by their customer until some time later. Contractors in the second category must normally part with their money only after they have been paid the tax by their customers. This difference in timing would, by itself, raise a troublesome issue of discrimination under the Supremacy Clause. This possible discrimination, however, is more than compensated for by the lower tax base. If it were not, the State would obviously put all contractors in the first category. Moreover, if this problem were to become a serious one in any given case, it could be easily eliminated by having the Government buy the materials directly, in which case the contractor would become liable for payment of the tax—in this case, a use tax rather than a sales tax—at a later time; *i.e.*, at the time he uses those materials.

services. It is the state's major producer of revenue, and its impact is felt by almost everyone in the state—by the purchaser of lumber for an improvement to one's home, by the purchaser of clothes, furniture and even groceries.[29] A broader and more effective political check can hardly be imagined.[30]

V. The Test for Discrimination Established in Fresno, Which Requires Consideration of the Operative Effect of a State's Tax System as a Whole, is Consistent with the Tests for Discrimination Developed and Applied in Other Areas.

The issue of whether a state's tax system is discriminatory has risen in a variety of areas, the major ones being (in addition to that involved here) the area of interstate commerce and the area of taxation of national banks. And in resolving discrimination issues arising under the Supremacy Clause, the Court has looked for guidance to the principles established in those other two areas. See, *e.g.*, the Court's use of an interstate commerce case, *Henneford v. Silas Mason Co.*, 300 U.S. 577 (1937), in *Detroit*, 355 U.S. 466, 474, and its use of a national bank case, *Tradesman Bank v. Tax Comm'n*, 309 U.S. 560 (1940), in *Phillips Petroleum Co. v. Dumas School Dist.*, 361 U.S. 376, 383 (1960).

To take up the interstate commerce area first. In

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[29]The tax has even been extended to all food items. See, § 30, chapter 35, 1982 Wash. Laws. In the Brief of Amicus Curiae Multistate Tax Commission in Support of Jurisdictional Statement in this case it is stated that non-restaurant food items are exempt. See, MTC Br. 17, n. 6. Though true at the time, it is no longer true.

[30]In this regard, the last sentence in note 11 in *Fresno* should be noted. It reads:

> "This danger [of destroying a federal function] would never arise, however, if the tax is also imposed on the income and property interests of all other residents and voters of the State." 429 U.S. 452, 463, n. 11.

This seems to suggest that it was California's entire property tax system which provided the political check. Washington's sales and use tax system provides an equally extensive check here.

Southern Pacific Co. v. Gallagher, 306 U.S. 167 (1939), the California use tax was challenged as applied to personal property purchased outside the State but brought into the state for use there. The argument was based on California's tax structure, which placed the legal incidence of the sales tax on the seller, but the legal incidence of the use tax on the buyer or user. As stated by the Court:

> "* * * A discrimination against goods of out-of-state origin on the face of the sales and use acts is suggested because the local retailer may absorb the sales tax while the consumer of an imported article must pay the use tax. [Footnote omitted.] *But this is not a discrimination in the law.* California's exaction for the distribution of tangible personal property is the same, whether purchased within or without her borders or whether paid by the retailer or consumer. There is an equal charge against what is used, whatever its source. * * *" 306 U.S. at 172. (Emphasis supplied.)

Thus, the switch in legal incidence made no constitutional difference. Nor should it here.

In *Michigan National Bank v. Michigan*, 365 U.S. 467 (1961), the issue was whether a state tax on national banks was discriminatory under Rev. Stat. § 5219, 12 U.S.C. § 548, which, as it then read, prohibited a state tax on national bank shares at a greater rate than was imposed upon "other moneyed capital." The bank contended that Michigan was discriminating against national banks, as compared with savings and loan associations, with which they were in competition. In rejecting that contention, the Court said:

> "While it is obvious that the taxable value of the shares in these two types of financial institutions is determined by different methods [footnote omitted] and that they are being taxed at different rates, it does not follow that § 5219 is automatically violated. '[I]t is not a valid objection to a tax on national bank shares that other moneyed capital in the state [is] * * * taxed at a different method unless it appears that the difference in treatment results in fact in a discrimination unfavorable to the holders of the

shares of national banks.' Tradesmens Nat. Bank v Oklahoma Tax Com., supra, (309 US at 567). * * *" 365 U.S. at 478, 479.

The Court compared the practical effects of these two different sets of taxes, and found no discrimination. A similar approach, which focuses on the operative effects of the differences in tax treatment, should be taken here with a similar result.

CONCLUSION

This case presents something of a legal jigsaw puzzle. But all of the pieces can be properly fitted together, with none left out, in the manner required by this Court's prior decisions. And once this is done, the conclusion is clear: Washington's system for taxing federal contractors does not violate the Supremacy Clause, and accordingly the judgment of the Court of Appeals should be reversed.

Respectfully submitted,

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APPENDIX A

State Statutes

Washington Session Laws*

*Emphasis original, representing amendatory language in the session laws. Language deleted by amendments is shown in parentheses.

Chapter 90, 1975 Wash. Laws (Substitute House Bill No. 86), §§ 1-5, amending Wash. Rev. Code §§ 82.04.050, 82.04.190, and 82.04.280(7).

Section 1. Section 1, chapter 8, Laws of 1970 ex. sess. as last amended by section 1, chapter 145, Laws of 1973 1st ex. sess. and RCW 82.04.050 are each amended to read as follows:

"Sale at retail" or "retail sale" means every sale of tangible personal property (including articles produced, fabricated, or imprinted) to all persons irrespective of the nature of their business and including, among others, without limiting the scope hereof, persons who install, repair, clean, alter, improve, construct, or decorate real or personal property of or for consumers other than a sale to a person who (a) purchases for the purpose of resale as tangible personal property in the regular course of business without intervening use by such person, or (b) installs, repairs, cleans, alters, imprints, improves, constructs, or decorates real or personal property of or for consumers, if such tangible personal property becomes an ingredient or component of such real or personal property without intervening use by such person, or (c) purchases for the purpose of consuming the property purchased in producing for sale a new article of tangible personal property or substance, of which such property becomes an ingredient or component or is a chemical used in processing, when the primary purpose of such chemical is to create a chemical reaction directly through contact with an ingredient of a new article being produced for sale. The term shall include every sale of tangible personal property which is used or consumed or to be used or consumed in the performance of any activity classified as a "sale at retail" or "retail sale" even though such property is resold

or utilized as provided in (a), (b), or (c) above following such use. The term also means every sale of tangible personal property to persons engaged in any business which is taxable under RCW 82.04.280, subsections (2) and (7) and RCW 82.04.290.

* * *

The term shall also include the renting or leasing of tangible personal property to consumers.

* * *

The term shall not include the sale of or charge made for labor and services rendered in respect to the building, repairing, or improving of any street, place, road, highway, easement, right of way, mass public transportation terminal or parking facility, bridge, tunnel, or trestle which is owned by a municipal corporation or political subdivision of the state or by the United States and which is used or to be used primarily for foot or vehicular traffic including mass transportation vehicles of any kind, nor shall it include sales of feed, seed, fertilizer, and spray materials to persons for the purpose of producing for sale any agricultural product whatsoever, including milk, eggs, wool, fur, meat, honey, or other substances obtained from animals, birds, or insects but only when such production and subsequent sale are exempt from tax under RCW 82.04.330, nor shall it include sales of chemical sprays or washes to persons for the purpose of post-harvest treatment of fruit for the prevention of scald, fungus, mold, or decay.

The term shall not include the sale of or charge made for tangible personal property consumed and/or for labor and services rendered in respect to the constructing, repairing, decorating, or improving of new or existing buildings or other structures under, upon, or above real property of or for the United States, any instrumentality thereof, or a county or city housing authority created pursuant to chapter 35.82 RCW, including the installing, or attaching of any article of tangible personal property therein or thereto, whether or not such personal property

becomes a part of the realty by virtue of installation. Nor shall the term include the sale of services or charges made for the clearing of land and the moving of earth of or for the United States, any instrumentality thereof, or a county or city housing authority.

Sec. 2. Section 82.04.190, chapter 15, Laws of 1961 as last amended by section 4, chapter 299, Laws of 1971 ex. sess. and RCW 82.04.190 are each amended to read as follows:

"Consumer" means the following:

(1) Any person who purchases, acquires, owns, holds, or uses any article of tangible personal property irrespective of the nature of his business and including, among others, without limiting the scope hereof, persons who install, repair, clean, alter, improve, construct, or decorate real or personal property of or for consumers other than for the purpose (a) of resale as tangible personal property in the regular course of business or (b) of incorporating such property as an ingredient or component of real or personal property when installing, repairing, cleaning, altering, imprinting, improving, constructing, or decorating such real or personal property of or for consumers or (c) of consuming such property in producing for sale a new article of tangible personal property or a new substance, of which such property becomes an ingredient or component or as a chemical used in processing, when the primary purpose of such chemical is to create a chemical reaction directly through contact with an ingredient of a new article being produced for sale;

(2) Any person engaged in any business activity taxable under RCW 82.04.290;

(3) Any person engaged in the business of contracting for the building, repairing or improving of any street, place, road, highway, easement, right of way, mass public transportation terminal or parking facility, bridge, tunnel, or trestle which is owned by a municipal corporation or political subdivision of the state of Washington or by the United States and which is used or to be used primarily for foot or vehicular traffic including mass transportation

vehicles of any kind as defined in RCW 82.04.280, in respect to tangible personal property when such person incorporates such property as an ingredient or component of such publicly owned street, place, road, highway, easement, right of way, mass public transportation terminal or parking facility, bridge, tunnel, or trestle by installing, placing or spreading the property in or upon the right of way of such street, place, road, highway, easement, bridge, tunnel, or trestle or in or upon the site of such mass public transportation terminal or parking facility;

(4) Any person who is an owner, lessee or has the right of possession to or an easement in real ((~~or personal~~)) property which is being constructed, repaired, decorated, improved, ((~~cleaned, imprinted,~~)) or otherwise altered by a person engaged in business, excluding only ((~~the United States and~~)) (a) municipal corporations or political subdivisions of the state in respect to labor and services rendered to their real property which is used or held for public road purposes, and (b) the United States, instrumentalities thereof, and county and city housing authorities created pursuant to chapter 35.82 RCW in respect to labor and services rendered to their real property. Nothing contained in this or any other subsection of this definition shall be construed to modify any other definition of "consumer";

(5) Any person who is an owner, lessee, or has the right of possession to personal property which is being constructed, repaired, improved, cleaned, imprinted, or otherwise altered by a person engaged in business;

(6) Any person engaged in the business of constructing, repairing, decorating, or improving new or existing buildings or other structures under, upon, or above real property of or for the United States, any instrumentality thereof, or a county or city housing authority created pursuant to chapter 35.82 RCW, including the installing or attaching of any article of tangible personal property therein or thereto, whether or not such personal property becomes a part of the realty by virtue of installation. Any such person shall be a consumer within

the meaning of this subsection in respect to tangible personal property incorporated into, installed in, or attached to such building or other structure by such person.

Sec. 3. Section 2, chapter 8, Laws of 1970 ex. sess. as last amended by section 5, chapter 299, Laws of 1971 ex. sess. and RCW 82.04.280 are each amended to read as follows:

Upon every person engaging within this state in the business of: (1) Printing, and of publishing newspapers, periodicals or magazines; (2) building, repairing or improving any street, place, road, highway, easement, right of way, mass public transportation terminal or parking facility, bridge, tunnel, or trestle which is owned by a municipal corporation or political subdivision of the state or by the United States and which is used or to be used, primarily for foot or vehicular traffic including mass transportation vehicles of any kind and including any readjustment, reconstruction or relocation of the facilities of any public, private or cooperatively owned utility or railroad in the course of such building, repairing or improving, the cost of which readjustment, reconstruction, or relocation, is the responsibility of the public authority whose street, place, road, highway, easement, right of way, mass public transportation terminal or parking facility, bridge, tunnel, or trestle is being built, repaired or improved; (3) extracting for hire or processing for hire; (4) operating a cold storage warehouse, but not including the rental of cold storage lockers; (5) representing and performing services for fire or casualty insurance companies as an independent resident managing general agent licensed under the provisions of RCW 48.05.310; (6) radio and television broadcasting, excluding network, national and regional adverstising computed as a standard deduction based on the national average thereof as annually reported by the Federal Communications Commission, or in lieu thereof by itemization by the individual broadcasting station, and excluding that portion of revenue represented by the out-of-state

audience computed as a ratio to the station's total audience as measured by the 100 micro-volt signal strength and delivery by wire, if any; (7) engaging in activities which bring a person within the definition of consumer contained in RCW 82.04.190(6), as now or hereafter amended; as to such persons, the amount of tax on such business shall be equal to the gross income of the business mutiplied by the rate of forty-four one hundredths of one percent.

NEW SECTION. Sec. 4. In the event any person has entered into a contract prior to July 1, 1975 or has bid upon a contract prior to July 1, 1975 and has been awarded the contract after July 1, 1975 and would be required under the terms of the contract to bear the economic burden of the additional taxes imposed by this 1975 amendatory act, the additional taxes imposed by this 1975 amendatory act shall not be required to be paid by such person in carrying on activities in the fulfillment of such contract.

NEW SECTION. Sec. 5. This 1975 amendatory act is necessary for the immediate preservation of public peace, health and safety, the support of the state government and its existing public institutions, and shall take effect July 1, 1975.

Passed the House March 14, 1975.
Passed the Senate May 19, 1975.
Approved by the Governor May 27, 1975.
Filed in Office of Secretary of State May 27, 1975.

Chapter 291, 1975, Wash. Laws 1st Ex. Sess. (Engrossed Substitute Senate Bill No. 2736) § 5, amending Wash. Rev. Code § 82.04.050.

* * *

Sec. 5. Section 1, chapter 8, Laws of 1970 ex. sess. as last amended by section 1, chapter 90, Laws of 1975 1st ex. sess. and RCW 82.04.050 are each amended to read as follows:

"Sale at retail" or "retail sale" means every sale of tangible personal property (including articles produced, fabricated, or imprinted) to all persons irrespective of the nature of their business and including, among others, without limiting the scope hereof, persons who install, repair, clean, alter, improve, construct, or decorate real or personal property of or for consumers other than a sale to a person who (a) purchases for the purpose of resale as tangible personal property in the regular course of business without intervening use by such person, or (b) installs, repairs, cleans, alters, imprints, improves, constructs, or decorates real or personal property of or for consumers, if such tangible personal property becomes an ingredient or component of such real or personal property without intervening use by such person, or (c) purchases for the purpose of consuming the property purchased in producing for sale a new article of tangible personal property or substance, of which such property becomes an ingredient or component or is a chemical used in processing, when the primary purpose of such chemical is to create a chemical reaction directly through contact with an ingredient of a new article being produced for sale. The term shall include every sale of tangible personal property which is used or consumed or to be used or consumed in the performance of any activity classified as a "sale at retail" or "retail sale" even though such property is resold or utilized as provided in (a), (b), or (c) above following such use. The term also means every sale of tangible personal property to persons engaged in any business which is taxable under RCW 82.04.280, subsections (2) and (7) and RCW 82.04.290.

* * *

The term shall not include the sale of or charge made for ((~~tangible personal property consumed and/or for~~)) labor and services rendered in respect to the constructing, repairing, decorating, or improving of new or existing buildings or other structures under, upon, or above real property of or for the United States, any instrumentality

thereof, or a county or city housing authority created pursuant to chapter 35.82 RCW, including the installing, or attaching of any article of tangible personal property therein or thereto, whether or not such personal property becomes a part of the realty by virtue of installation. Nor shall the term include the sale of services or charges made for the clearing of land and the moving of earth of or for the United States, any instrumentality thereof, or a county or city housing authority.

* * *

Passed the Senate June 9, 1975.
Passed the House June 9, 1975.
Approved by the Governor July 2, 1975.
Filed in the Office of Secretary of State July 2, 1975.

Chapter 1, 1975-76 Wash. Laws 2nd Ex. Sess. (House Bill No. 1229), amending Wash. Rev. Code §§ 82.12.010 and 82.12.020.

Section 1. Section 82.12.010, chapter 15, Laws of 1961 as last amended by section 52, chapter 278, Laws of 1975 1st ex. sess. and RCW 82.12.010 are each amended to read as follows:

For the purposes of this chapter:

(1) "Value of the article used" shall mean the consideration, whether money, credit, rights, or other property, expressed in terms of money, paid or given or contracted to be paid or given by the purchaser to the seller for the article of tangible personal property, the use of which is taxable under this chapter. The term includes, in addition to the consideration paid or given or contracted to be paid or given, the amount of any tariff or duty paid with respect to the importation of the article used. In case the article used is acquired by lease or by gift or is extracted, produced, or manufactured by the person using the same or is sold under conditions wherein the purchase price does not represent the true value thereof, the value of the article used shall be determined as nearly

as possible according to the retail selling price at place of use of similar products of like quality and character under such rules and regulations as the department of revenue may prescribe.

In case the articles used are acquired by bailment, the value of the use of the articles so used shall be in an amount representing a reasonable rental for the use of the articles so bailed, determined as nearly as possible according to the value of such use at the places of use of similar products of like quality and character under such rules and regulations as the department of revenue may prescribe ((;)): PROVIDED, That in case any such articles of tangible personal property are used in respect to the construction, repairing, decorating, or improving of, and which become or are to become an ingredient or component of, new or existing buildings or other structures under, upon, or above real property of or for the United States, any instrumentality thereof, or a county or city housing authority created pursuant to chapter 35.82 RCW, including the installing or attaching of any such articles therein or thereto, whether or not such personal property becomes a part of the realty by virtue of installation, then the value of the use of such articles so used shall be determined according to the retail selling price of such articles, or in the absence of such a selling price, as nearly as possible according to the retail selling price at place of use of similar products of like quality and character or, in the absence of either of these selling price measures, such value may be determined upon a cost basis, in any event under such rules and regulations as the department of revenue may prescribe.

In the case of articles manufactured or produced by the user and used in the manufacture or production of products sold or to be sold to the department of defense of the United States, the value of the articles used shall be determined according to the value of the ingredients of such articles.

(2) "Use," "used," "using," or "put to use" shall have their ordinary meaning, and shall mean the first act within

this state by which the taxpayer takes or assumes dominion or control over the article of tangible personal property (as a consumer), and include installation, storage, withdrawal from storage, or any other act preparatory to subsequent actual use or consumption within this state;

(3) "Taxpayer" and "purchaser" include all persons included within the meaning of the word "buyer" and the word "consumer" as defined in chapters 82.04 and 82.08 RCW;

(4) "Retailer" means every person engaged in the business of selling tangible personal property at retail and every person required to collect from purchasers the tax imposed under this chapter;

(5) The meaning ascribed to words and phrases in chapters 82.04 and 82.08 RCW, insofar as applicable, shall have full force and effect with respect to taxes imposed under the provisions of this chapter. "Consumer," in addition to the meaning ascribed to it in chapters 82.04 and 82.08 RCW insofar as applicable, shall also mean any person who distributes or displays, or causes to be distributed or displayed, any article of tangible personal property, except newspapers, the primary purpose of which is to promote the sale of products or services.

Sec. 2. Section 82.12.020, chapter 15, Laws of 1961 as last amended by section 10, chapter 281, Laws of 1971 ex. sess. and RCW 82.12.020 are each amended to read as follows:

There is hereby levied and there shall be collected from every person in this state a tax or excise for the privilege of using within this state as a consumer any article of tangible personal property purchased at retail, or acquired by lease, gift, repossession, or bailment, or extracted or produced or manufactured by the person so using the same, or otherwise furnished to a person engaged in any business taxable under RCW 82.04.280, subsections (2) or (7). This tax will not apply with respect to the use of any article of tangible personal property purchased, extracted, produced or manufactured outside this state until the transportation of such article has finally ended or

until such article has become commingled with the general mass of property in this state. This tax shall apply to the use of every article of tangible personal property, including property acquired at a casual or isolated sale, and including byproducts used by the manufacturer thereof, except as hereinafter provided, irrespective of whether the article or similar articles are manufactured or are available for purchase within this state. Except as provided in subdivision (2) of RCW 82.12.030, payment by one purchaser or user of tangible personal property of the tax imposed by chapter 82.08 or 82.12 RCW shall not have the effect of exempting any other purchaser or user of the same property from the taxes imposed by such chapters. The tax shall be levied and collected in an amount equal to the value of the article used by the taxpayer multiplied by the rate of four and one-half percent.

Sec. 3. Section 4, chapter 90, Laws of 1975 1st ex. sess. is amended to read as follows:

In the event any person has entered into a contract prior to July 1, 1975 or has bid upon a contract prior to July 1, 1975 and has been awarded the contract after July 1, 1975 ((~~and would be required under the terms of the contract to bear the economic burden of the additional taxes imposed by this 1975 amendatory act~~)), the additional taxes imposed by chapter 90, Laws of 1975 1st ex. sess., section 5, chapter 291, Laws of 1975 1st ex. sess. and this 1975 amendatory act shall not be required to be paid by such person in carrying on activities in the fulfillment of such contract.

NEW SECTION. Sec. 4. If any provision of this 1975 amendatory act or its application to any person or circumstance is held invalid, the remainder of the act or the application of the provision to other persons or circumstances is not affected.

NEW SECTION. Sec. 5. This 1975 amendatory act is necessary for the immediate preservation of the public peace, health, and safety, the support of the state

government and its existing public institutions, and shall take effect immediately.

Passed the House July 20, 1975.
Passed the Senate July 19, 1975.
Approved by the Governor July 25, 1975.
Filed in Office of Secretary of State July 25, 1975.

APPENDIX B

State Administrative Regulations

WAC 458-20-198 (Rule 198) CONDITIONAL AND INSTALLMENT SALES, METHOD OF REPORTING

BUSINESS AND OCCUPATION TAX

Persons making conditional sales or other installment sales of tangible personal property must report the total selling price of such sales in the tax reporting period in which the sale is made.

A deduction from gross proceeds of sales as a credit loss is allowed to such sellers for the amount of the unpaid balance of the contract price on any installment sale if and when the property purchased is repossessed upon default by the buyer.

RETAIL SALES TAX, USE TAX

Persons making conditional sales or other installment sales of tangible personal property must report the total selling price of such sales in the tax period in which the sale is made.

The foregoing is true irrespective of the fact that such sellers arrange to receive payment of tax in installments or that a contract may be discounted or pledged with or sold to a finance company. In the latter case, although as a part of the agreement with the seller the finance company actually makes collection of the tax from the buyer as the installments fall due, the finance company should not report to the Department of Revenue the amount of tax collected since the total tax already has been reported by the seller.

No deduction for credit losses in case of repossessions is allowed under the retail sales tax or use tax.

Brief for the United States

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No. 81-969

In the Supreme Court of the United States

OCTOBER TERM, 1982

STATE OF WASHINGTON, ET AL., APPELLANTS

v.

UNITED STATES OF AMERICA

ON APPEAL FROM THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE UNITED STATES

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QUESTION PRESENTED

Whether Washington sales and use taxes imposed on federal construction project contractors unconstitutionally discriminate against the United States and those with whom it deals because similarly situated contractors engaged on private construction projects and on state construction projects are not so taxed.

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In the Supreme Court of the United States

OCTOBER TERM, 1982

No. 81-969

STATE OF WASHINGTON, ET AL., APPELLANTS

v.

UNITED STATES OF AMERICA

ON APPEAL FROM THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE UNITED STATES

OPINIONS BELOW

The decision and order of the district court (J.S. App. C-1 to C-3) is not officially reported. The opinion of the court of appeals (J.S. App. A-1 to A-15) is reported at 654 F.2d 570.

JURISDICTION

The judgment of the court of appeals was entered on August 24, 1981 (J.S. App. B-1). The notice of appeal (J.S. App. F-1 to F-3) was filed on November 16, 1981 (J.A. 4). The jurisdictional statement was filed on November 20, 1981, and probable jurisdiction was noted on May 17, 1982 (J.A. 68).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The relevant portions of Article VI of the United States Constitution and of chapters 82.04, 82.08 and 82.12 of the Wash. Rev. Code Ann. (1981), as amended by 1975 Wash. Laws, chapters 90 and 291, Section 5, and as amended by 1975-1976 Wash. Laws, chapter 1, are set forth at J.S. App. G-1 and H-1 to H-8. The relevant provisions of chapter 82.14 of the Wash. Rev. Code Ann. (1981) are set forth in App. 1a-2a to the Motion to Affirm.

STATEMENT

A. The Statutory Background

1. During the period in question, the State of Washington, pursuant to chapters 82.04, 82.08, 82.12 and 82.14 of Wash. Rev. Code (1981),[1] levied a sales tax and a use tax, and authorized local counties and cities to levy sales and use taxes, on every retail sale of, and consumer use of, personal property in the state. Those taxes were required to be paid by the buyer or consumer. In the years immediately prior to July 1, 1975, the sales and use tax statutes defined the terms "retail sale," "buyer" and "consumer" in a manner that provided that, with respect to material incorporated in non-road construction projects[2] on real property, the transaction under the prime con-

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[1] Hereinafter the Wash. Rev. Code Ann. will be cited as RCW.

[2] Prior to July 1, 1975, RCW § 82.04.190(3) defined the term "consumer" as including a general contractor on a road-building project owned by the United States, a municipal corporation, or a political subdivision of the State, but did not include general contractors on road-building projects owned by the State or private entities.

tract between the owner of the realty and the prime contractor constituted the only "retail sale." Furthermore, the owner of the realty was the "consumer" who had the duty to pay any sales or use tax on the construction project. Under the then-existing statute, neither suppliers of material, subcontractors, nor the prime contractor paid any sales or use tax on the construction project or with respect to material incorporated in the building construction project. Accordingly, prior to July 1, 1975, no sales or use taxes were levied on non-road construction projects on real property owned by the federal government in the State of Washington or on the material incorporated in such construction projects because of the immunity of the United States from state taxes under the Supremacy Clause of the United States Constitution.[3]

In an attempt to collect sales and use taxes with respect to material incorporated in building construction projects owned by the United States, the Washington Legislature in 1975 redefined the terms "retail sale" and "consumer" in its sales and use tax statutes.[4] As a result, prime contractors performing con-

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[3] See *Kern-Limerick, Inc.* v. *Scurlock*, 347 U.S. 110 (1954); *McCulloch* v. *Maryland*, 17 U.S. (4 Wheat.) 316 (1819); *First Agricultural National Bank* v. *State Tax Commission*, 392 U.S. 339, 348 (1968).

[4] See Substitute House Bill No. 86, enacted into law effective July 1, 1975, as 1975 Wash. Laws, 1st Ex. Sess., ch. 90 (Appellant Br. App. 1a-6a). This statute amended RCW Section 82.04.050 (J.S. App. H-1) and 82.04.190 (J.S. App. H-2 to H-3).

See § 5 of Substitute Senate Bill No. 2736, enacted into law, effective July 2, 1975, as 1975 Wash. Laws, 1st Ex. Sess., ch. 291, § 5 (Appellant Br. App. 6a-8a). This statute also amended RCW Section 82.04.050 (J.S. App. H-1).

See House Bill No. 1229, enacted into law as 1975-1976 Wash. Laws, 2d Ex. Sess., ch. 1 (Appellant's Br. App. 8a-

struction work on real property owned by the United States were required to pay sales and use taxes on material and personal property incorporated into such construction projects.[5] Those statutes, however, did not amend the State's sales and use tax laws so as to impose any sales or use taxes on contractors performing construction work on real property owned by private persons or the State of Washington. With respect to those non-federal construction projects, any sales or use taxes imposed on the project or material incorporated in the project remained the obligation of the project's owner.

Thus, prime contractors performing construction work on real property in the State of Washington were divided into two broad categories: (1) prime contractors performing construction work for the United States and certain essentially federally-financed operations of local governments, who were liable for sales and use taxes on material incorporated into the construction project; and (2) prime contractors performing construction work for the state and private persons, who were not liable for any

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12a). This statute amended RCW Sections 82.12.010 (J.S. App. H-5 to H.7) and 82.12.020 (J.S. App. H-7 to H-8).

[5] The 1975 amendment also required general contractors to pay sales and use taxes on material and personal property incorporated in construction projects owned by city or county housing authorities. This change was made because the costs of these housing projects were financed by the federal government (J.A. 46-48) and because federal statutes required these projects to be exempt from state and local government taxation to qualify for federal aid. See *Housing Authority of Seattle* v. *Washington*, 629 F.2d 1307 (9th Cir. 1980); 42 U.S.C. 1437d(d).

sales or use taxes on the project or with respect to material incorporated in the project—with such taxes to be paid by the State or private person.[6]

2. The United States Department of the Navy and the United States Army Corps of Engineers have engaged in numerous construction projects in the State of Washington (J.A. 19-21, 33-35). Pursuant to the 1975 amendments to the Washington sales and use tax laws, officials of that State have required prime contractors on these and other United States Government construction projects to pay state sales and use taxes as "consumers" with respect to material incorporated in their federal construction projects (J.A. 44-45, 60-61). By contrast, similarly situated prime contractors for state and private persons are not so taxed (J.A. 51, 60-61). The affected federal agencies objected to these Washington sales and use taxes, and instructed their prime contractors to exclude all charges for these taxes from their contract bids, and to bill the United States separately for those taxes which they have been required to pay (J.A. 21, 34-35).

B. The Proceedings in this Case

1. Shortly after the 1975 amendments to the Washington tax statutes became effective, the United States commenced this suit in the United States District Court for the Western District of Washington. The suit sought: (1) a declaratory judgment that the

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[6] A contractor on a non-federally owned construction project is defined as a "seller" and is required to collect a sales tax from the owner of the project, who is defined as the "consumer," and to remit this collected tax to the State under RCW Section 82.08.050 (J.S. App. H-4). No use taxes, however, are collected or remitted to the State by construction contractors on non-federally owned construction projects.

state tax statutes were unconstitutional under the Supremacy Clause as applied to the United States and its contractors; (2) a permanent injunction against the assessment and collection of those taxes from federal contractors; and (3) a judgment refunding to the United States all of the state sales and use taxes which had been collected by the State since July 1, 1975, from prime contractors engaged in construction projects on real property owned by the United States, and with respect to which the United States had reimbursed its prime contractors (J.S. App. A-6; J.A. 5-8).

Thereafter, the United States filed a motion for partial summary judgment seeking, *inter alia*, a declaration that chapters 82.08, 82.12 and 82.14 of the Wash. Rev. Code Ann., as amended, unconstitutionally discriminated against the United States and its contractors, because those sales and use taxes were imposed and levied upon prime construction contractors with respect to construction projects for the United States, and no similar taxes were levied upon prime construction contractors with respect to construction projects for private individuals or the State of Washington and its various agencies (J.S. App. A-7; J.A. 14-16). In response, the State cross-moved for summary judgment and sought dismissal of the complaint (J.A. 62).[7]

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[7] The case was filed prior to the August 12, 1976 repeal of 28 U.S.C. 2281, and sought a declaration of the unconstitutionality of a state statute. Accordingly, the government applied for a three-judge federal district court to rule upon the motions (J.S. App. A-7). Before the application was acted upon, the parties stipulated to the dismissal of the original action, which was subsequently refiled along with the pleadings then on file, which were all deemed refiled as of May 12, 1977. This procedure brought the case under the

The district court denied the State's motion and awarded partial summary judgment to the government. It ruled, *inter alia*, (1) that the provisions of RCW chapters 82.04, 82.08, 82.12 and 82.14 imposing sales and use taxes only on contractors for the United States discriminated against contractors who deal with the United States and therefore violated the Supremacy Clause; (2) that the legal incidence of the Washington sales and use taxes fell upon the contractor and not upon the United States; and (3) that the imposition of the use tax upon contractors with respect to materials furnished to them by the United States for their use in connection with federal construction projects, but not for incorporation in those projects, was constitutionally permissible insofar as that same use tax was imposed upon contractors working on state or private projects. The district court enjoined the assessment and collection of the taxes found invalid and severed the question as to the validity of the taxes from the amount of any refund for a separate trial (J.S. App. C-1 to C-3, D-1 to D-3).

2. The court of appeals affirmed (J.S. App. A-1 to A-15, B-1). It ruled that in considering whether the Washington taxing statutes unconstitutionally discriminated against the federal government and those with whom it deals, the relevant group of similarly situated persons was the body of all prime contractors, and not all "consumers," as the State suggested. The court ruled that "[w]hat must be examined is whether prime contractors on federal projects are disadvantaged in comparison to prime con-

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amended version of Section 2281 and thereby avoided the necessity of convening a three-judge district court (J.S. App. A-7; J.A. 1).

tractors on non-federal projects" (J.S. App. A-11). In so concluding, the court reasoned (J.S. App. A-12):

> Because no contractors except those dealing with the United States are taxed, or necessarily have another's tax burden economically shifted to them, as occurred in *Fresno* [*United States* v. *County of Fresno*, 429 U.S. 452 (1977)] and *Detroit* [*United States* v. *City of Detroit*, 355 U.S. 466 (1958)], federal contractors are financially disadvantaged in a way that has the constitutionally impermissible potential of interfering with the functions of the federal government. The State's preferential treatment of prime contractors on non-federal projects could discourage contractors from performing work for the United States or could lead to their doing so only at higher levels of compensation than demanded for comparable non-federal work. * * * If a tax treats those dealing with the United States in a more disadvantageous fashion than those not dealing with it, as do these taxes, the potential for interfering with the functioning of the federal government has been unconstitutionally created.

Furthermore, the court of appeals found that no political check was available to protect the federal contractors from abusive taxation because "all prime contractors were [not] forced either directly or indirectly to pay the challenged taxes" (J.S. App. A-13).

Finally, the court of appeals rejected the State's contention that by forcing the federal government to reimburse its contractors for the taxes imposed upon them, the taxing scheme was constitutional because the State imposed upon the federal government no

greater burden than it imposed upon other purchasers of construction work (J.S. App. A-14). The court explained that "[t]he challenged statutes cannot be made valid by equalizing the tax burden of the United States with that of non-federal owners of real property on which construction work is done because a tax either directly imposed on the federal government or indirectly passed on to it by contractors would be constitutionally impermissible as a tax on the United States without its consent" (*ibid.*).

SUMMARY OF ARGUMENT

1. This Court has consistently held that "a tax may be invalid even though it does not fall directly on the United States if it operates so as to discriminate against the Government or those with whom it deals." *United States* v. *City of Detroit*, 355 U.S. 466, 473 (1958). This proscription against taxes that discriminate against the United States or those with whom it deals is inherent in, and a vital part of, the federal government's immunity from state taxation under the Supremacy Clause of the United States Constitution. Thus, if a state tax is imposed upon those who deal with the federal government and is not "imposed equally on the other similarly situated constituents of the States" (*United States* v. *County of Fresno*, 429 U.S. 452, 462 (1977)), the tax is discriminatory and may not be constitutionally applied to those who deal with the federal government. See, *e.g.*, *McCulloch* v. *Maryland*, 17 U.S. (4 Wheat.) 316 (1819); *Moses Lake Homes, Inc.* v. *Grant County*, 365 U.S. 744, 751 (1961); *Phillips Chemical Co.* v. *Dumas School District*, 361 U.S. 376, 387 (1960); *United States* v. *New Mexico*, No. 80-702 (Mar. 24, 1982), slip op. 14 n.11.

This case presents a classic example of the imposition of discriminatory taxes on those who deal with the United States. In the years immediately prior to July 1, 1975, contractors dealing with the federal and state governments and with private parties in the State of Washington were not liable for sales or use taxes on materials and services incorporated into construction projects. Rather, the State of Washington imposed sales or use taxes upon property owners, including state and local governments, with respect to the cost of construction projects on their property. Because of "the unavoidable consequence of that supremacy which the constitution has declared" (*McCulloch* v. *Maryland*, *supra*, 17 U.S. (4 Wheat.) at 436 (1819)), the federal government was immune from these taxes on the cost of construction work done for it. Effective after June 30, 1975, however, the State of Washington amended its statutes specifically to gain revenue from federal government contracts, by imposing sales or use taxes upon contractors with respect to items incorporated in construction projects for the federal government. But the amended versions of the taxes were not imposed on contractors for private parties and state and local governments. The segregation of federal construction contractors for taxation was a purposeful attempt to circumvent the immunity of the United States that cannot pass muster under the Supremacy Clause of the Constitution. For a tax laid exclusively on those who deal with the United States is nothing more than a tax on the United States itself.

2. Our submission finds solid support in this Court's decisions in *Miller* v. *Milwaukee*, 272 U.S. 713 (1927); *Phillips Chemical Co.* v. *Dumas School District*, 361 U.S. 376 (1960); and *Moses Lake Homes*,

Inc. v. *Grant County*, 365 U.S. 744 (1961). Those cases establish that the Supremacy Clause bars a state from singling out those who deal with the United States for special tax burdens, either inadvertently or, as here, purposefully.

Contrary to the State's argument, the Supremacy Clause guarantees more than simply that the United States will not be placed at a competitive disadvantage. This Court established in *Moses Lake Homes* that discriminatory tax treatment against federal leases could not be cured, as the court of appeals mistakenly thought in that case, by equalizing the tax burdens on federal and non-federal lessees. The Court therefore held that the tax disparities against the federal lessees required the complete invalidation of the state tax against them.

Thus, the fact that private owners and the State were taxed on construction projects does not, as the State would have it, save the Washington tax from invalidity. As this Court pointed out in *United States* v. *County of Fresno*, *supra*, 429 U.S. at 458-459, the only protection that the United States and those with whom it deals have from abusive state taxation on persons who deal with the Unted States is the imposition of the tax upon similarly situated persons. Here, the persons similarly situated are the contractors performing construction for the federal government and the contractors working on privately or state-owned construction projects (see J.S. App. A-11). Furthermore, it is plain that the contractors who deal with the United States are subject to greater tax burdens than those who deal with the State and with private persons. In these circumstances, as the court of appeals correctly stated (J.S. App. A-13 to A-14 n.14), the necessary political safeguard to protect the contractors who deal with the federal government from

abusive taxation would be present only if the contractors who deal with the State and the private sector were similarly taxed. " * * * [I]t does not seem too much to require that the State treat those who deal with the Government as well as it treats those with whom it deals itself." *Phillips Chemical Co.* v. *Dumas School District, supra,* 361 U.S. at 385.

ARGUMENT

THE IMPOSITION OF WASHINGTON'S SALES AND USE TAXES UPON FEDERAL BUT NOT PRIVATE OR STATE CONTRACTORS VIOLATES THE CONSTITUTIONAL IMMUNITY OF THE UNITED STATES FROM STATE TAXATION BECAUSE IT DISCRIMINATES AGAINST THE UNITED STATES AND THOSE WITH WHOM IT DEALS

A. The Supremacy Clause of the Constitution Absolutely Immunizes the Federal Government from State Taxation and its Contractors from Discriminatory State Taxation

1. This case presents an important question as to the ability of a state to circumvent the absolute constitutional immunity of the United States from state taxation under the Supremacy Clause.

Article VI, Clause 2 of the United States Constitution prescribes that "This Constitution, and the laws of the United States which shall be made in Pursuance thereof; * * * shall be the Supreme Law of the Land * * *." This provision, commonly known as the Supremacy Clause, is the basis of the Court's landmark decision in *McCulloch* v. *Maryland,* 17 U.S. (4 Wheat.) 316 (1819), which expounded the principle that the property, functions, and instrumentalities of the federal government are immune from taxation by its constituent parts.

Since that time, "the Court has never questioned the propriety of absolute federal immunity from state taxation." *United States* v. *New Mexico*, No. 80-702, decided March 24, 1982, slip op. 12. In determining the reaches of that constitutional immunity, the Court has often considered whether property belonged to the United States under particular arrangements with private parties or whether particular entities were federal instrumentalities. But "[t]he one constant here, of course, is simple enough to express: a State may not, consistent with the Supremacy Clause, U.S. Const., Art. VI, cl. 2, lay a tax 'directly upon the United States.' *Mayo* v. *United States*, 319 U.S. 441, 447 (1943)" (*ibid.*). Federal tax immunity is "the unavoidable consequence of that supremacy which the constitution has declared." *McCulloch* v. *Maryland*, *supra*, 17 U.S. (4 Wheat.) at 436.

A corollary of the fundamental constitutional doctrine that the states may not lay a direct tax upon the United States, is the equally well-settled principle that "a tax may be invalid even though it does not fall directly on the United States if it operates so as to discriminate against the Government or those with whom it deals." *United States* v. *City of Detroit*, 355 U.S. 466, 473 (1958). Accord: *City of Detroit* v. *Murray Corp.*, 355 U.S. 489, 495 (1958); *Phillips Chemical Co.* v. *Dumas School District*, 361 U.S. 376, 383, 385 (1960); *Moses Lake Homes, Inc.* v. *Grant County*, 365 U.S. 744 (1961); *United States* v. *County of Fresno*, 429 U.S. 452, 463 n.11, 464 (1977). As the Court most recently reaffirmed in *United States* v. *New Mexico*, *supra*, slip op. 14 n.11, "It remains true, of course, that state taxes on contractors are constitutionally invalid if they discrimi-

nate against the Federal Government, or substantially interfere with its activities."

The principle that a state tax may not discriminate against the federal government or those with whom it deals is essential to the effective application of the tax immunity doctrine. Indeed, the prohibition against discrimination logically follows from the *McCulloch* principle forbidding direct state taxation of the federal government or its instrumentalities. For absent that prohibition, the states could easily circumvent the immunity of the United States against direct state taxation. It can hardly be doubted that a tax levied only on those who deal with the United States is equivalent to a direct tax on the United States.

In *McCulloch*, the Court struck down a Maryland tax laid directly upon the Bank of the United States in connection with the issuance of its notes. But in a recent reexamination of the basis of *McCulloch*, the Court also found it instructive that no similar tax was imposed on the issuance of notes by any other bank in Maryland. In such circumstances, "the political check against abuse of the power to tax a State's constituents is absent when the State taxes only a federal function (foonote omitted)." *United States* v. *County of Fresno*, *supra*, 429 U.S. at 458. "The rule to be derived from the Court's more recent decision, then, is that the economic burden on a federal function of a state tax imposed on those who deal with the Federal Government does not render the tax unconstitutional as long as the tax is imposed equally on the other similarly situated constituents of the State (footnote omitted)" (*id.* at 462).

Thus, where, as here, the federal government's contractors are singled out for a special tax that applies

to no other constituent contractor within the State, the tax also violates the Supremacy Clause just as if the tax were laid directly upon the United States. As the Court pointed out in *County of Fresno*, "A State's constituents can be relied on to vote out of office any legislature that imposes an abusively high tax on them. They cannot be relied upon to be similarly motivated when the tax is instead solely on a federal function" (*id.* at 458-459).

2. This case presents a classic example of the imposition of discriminatory taxes on those who deal with the United States. As we shall show, in the years immediately prior to July 1, 1975, contractors, whether dealing with the federal and state governments or with private parties in the State of Washington, were not liable for sales or use taxes on materials and services incorporated into construction projects. Rather, the State of Washington imposed sales or use taxes upon property owners, including state and local governments, with respect to the cost of construction projects on their property. Because of "the unavoidable consequence of that supremacy which the constitution has declared" (*McCulloch* v. *Maryland*, *supra*, 17 U.S. (4 Wheat.) at 436), the federal government was immune from these taxes on the cost of construction work done for it. Effective after June 30, 1975, however, the State of Washington amended its statutes specifically to gain revenue from federal government contracts, and imposed sales or use taxes upon construction projects for the federal government. Those taxes, however, were not imposed on contractors for private parties and state and local governments. The segregation of federal construction contractors for taxation was an admittedly purposeful attempt to circumvent the tax immunity of the United States that is a consequence of the Supremacy Clause of the

Constitution. Such discrimination is likewise barred by the Supremacy Clause. For "* * * [I]t still remains true, as it has from the time of *M'Culloch* v. *Maryland*, 4 Wheat. 316, that a state tax may not discriminate against the Government or those with whom it deals." *Phillips Chemical Co.* v. *Dumas School District*, *supra*, 361 U.S. at 387.

We turn now to a detailed analysis of this Court's decisions prohibiting discriminatory state taxation of federal contractors. These decisions demonstrate that the Washington sales and use tax statutes violate the constitutional immunity of the United States from state taxation.

B. The Decisions of this Court Establish that the Supremacy Clause Bars a State From Singling Out Those Who Deal With the United States for Special Tax Burdens

1. Three decisions of this Court point the way toward affirmance of the decision below holding that the Washington sales and use tax impermissibly seeks to circumvent the constitutional tax immunity of the United States by singling out federal contractors for discriminatory taxation.

More than 50 years ago in *Miller* v. *Milwaukee*, 272 U.S. 713 (1927), the Court struck down a Wisconsin tax that similarly sought to circumvent the tax immunity of the federal government. At issue was a Wisconsin corporate income tax that did not, as it could not (Rev. Stat. 3701), tax interest from bonds of the United States. Corporate dividends received by stockholders were generally not taxed, but if only part of a corporation's income was subject to tax, then only a corresponding part of the dividends it distributed was immunized from personal income tax upon the

recipient shareholders. Accordingly, the State sought to tax that fraction of corporate dividends equal to the fraction of the corporation's income derived from federal government bonds. Although generally "a corporation is a non-conductor that cuts off connection between dividends to its shareholders and the corporate funds from which the dividends are paid" (272 U.S. at 714), (cf. Treasury Regulations on Income Tax (1954 Code) (26 C.F.R.), Sec. 1312-6(b)), the Court held unconstitutional the State's attempt to single out the income from government bonds for state taxation. It was the selection of such income for tax, to the exclusion of other income, that was the basis of the decision. As the Court stated, "A system of taxation that applied to stockholders of all corporations equally might tax, we assume for purposes of argument, the stockholders of a corporation that had invested all its property in United States bonds. But it would be a different matter if the State selected such corporations, supposing a number of them to exist, and taxed their stockholders alone" (*id.* at 714-715).

Such discriminatory selectivity is forbidden by the Constitution. As a unanimous Court subsequently characterized *Miller*, "It is true that in *Miller* the ostensible incidence of the tax—shareholders' income from corporate dividends—was not itself exempt, but the measure of the tax excluded all income not attributable to federal bonds owned by the corporation; that was the defect in the tax." *Phillips Chemical Co.* v. *Dumas School District*, *supra*, 361 U.S. at 382. The Court therefore reaffirmed that *Miller* stands for the proposition that "a State may not single out those who deal with the Government, in one capacity or another, for a tax burden not imposed on others similarly situated" (*id.* at 383).

The Court's decision in *Phillips Chemical Co.* demonstrates that the discrimination against the federal government need not be explicit in state statutes to be prohibited by the Supremacy Clause. There, one Texas statute provided for taxation of private users of government realty, measured by the full value of the fee. A second provision imposed a tax at a lesser measure (the value of the leasehold) for property held under a lease for three years or more, and which belonged to the State or an exempt owner. It appeared, however, that only leases of public property qualified for this classification (361 U.S. at 380). The Texas courts had construed a lease for three years or more, but subject to termination by the lessor in the event of a sale, as a lease for less than three years. Since the federal lease in question was subject to termination in the event of sale, the lessee could not qualify for the preferential tax treatment and was taxed at full value. Accordingly, the Court held unconstitutional the statute under which the federal lessee was taxed. As the Court concluded, "Here, Phillips is taxed under Article 5248 on the full value of the real property which it leases from the Federal Government, while businesses with similar leases, using exempt property owned by the State and its political subdivisions, are not taxed on their leaseholds at all. * * * It follows that Article 5248, as applied in this case, discriminates unconstitutionally against the United States and its lessee" (361 U.S. at 387).

Moses Lake Homes, Inc. v. *Grant County, supra*, a case from the State of Washington, is to the same effect. There, the County had taxed Wherry Act leaseholds on property owned by the United States at rates higher than other leaseholds, including privately owned leaseholds on state land. The court of

appeals had held that the discrimination against those who dealt with the United States was unconstitutional, and had remanded the case with instructions for the district court to reduce the taxes on Wherry Act leaseholders to the level of those on other leaseholders. But this Court reversed—not because it sanctioned the State of Washington's discriminatory taxation of those who dealt with the United States—but because relief that simply removed the competitive disadvantage was inappropriate and inadequate. Instead, this Court held that the discriminatory tax upon the Wherry Act leaseholders was absolutely void. As the Court flatly concluded, "When, as here, the tax is invalid, it 'may not be exacted.'" *Phillips Co.* v. *Dumas School District*, 361 U.S. at 387." 365 U.S. at 752.

2. Each of the foregoing decisions supports our submission that the Washington tax is invalid as applied to the federal government's contractors. *Miller* v. *Milwaukee* long ago established that a state cannot single out the federal government and those with whom it deals for special tax burdens. Indeed, the present case follows *a fortiori* from *Miller* and *Phillips Chemical Co.*, since the State is entirely candid in conceding that the 1975 amendments to its sales and use tax statutes were a purposeful attempt to circumvent the immunity of the United States from state taxation. As it acknowledges (Br. 6-8), when Washington's sales and use taxes were first enacted in 1935, sales to building contractors were subject to tax, and the use of property by a contractor was subject to the use tax if the property had not been subjected to the sales tax. This rule was generally applicable to all contractors, so the economic burden of such a tax might be passed on to the United States and all other persons employing contractors, as would

be the case with a property tax and other taxes to which contractors with the United States might be subject. *James* v. *Dravo Contracting Co.*, 302 U.S. 134 (1937); *Alabama* v. *King & Boozer*, 314 U.S. 1 (1941).

Recognizing an opportunity for an enlarged base and enhanced revenue, the State in 1941 amended its statutes so that the sale by the contractor to the owner of the property became the taxable transaction, not the sale of materials or equipment to the contractor, or the contractor's use of such property. This shift enabled the State to include the value of the labor and services supplied by the contractor, and the contractor's profit in the enlarged tax base. But since the tax now fell upon the property owner who employed the contractor, the federal government's constitutional immunity prevented Washington from imposing its sales tax upon the United States with respect to its transactions with the contractors whom it employed.

For more than 30 years, the State apparently remained content with the choice it had made in the post-1941 structure of its sales tax to gain enhanced revenue from other sources at the price of sacrificing revenue from federal government contractors. By 1975, however, construction activity on behalf of the United States had substantially increased. Accordingly, the State sought to circumvent the tax immunity of the United States while retaining the value of the contractors' labor and services in the tax base. The result was the 1975 statutory amendments at issue here, by which the State imposes its sales and use tax upon contractors for the United States, but not upon contractors engaged in other construction for private parties or for the State.

The United States, like other entities, can act only through those who serve it in one capacity or another. Its immunity would mean little if, whenever a state law of general applicability had its legal incidence upon the United States, the State could then turn and enact parallel special legislation directed only to those who serve or deal with the United States. Cf. *United States* v. *Mississippi Tax Commission*, 412 U.S. 363 (1973); *United States* v. *Mississippi Tax Commission*, 421 U.S. 599 (1975). To single out for taxation those who serve the United States is to tax the United States itself.

C. The Sales and Use Taxes Seek Purposefully to Circumvent the Immunity of the United States by Discriminating Against Contractors Dealing With the United States

1. As we have pointed out (*supra*, pages 2-3), the State of Washington levied a sales tax on every retail sale in the State,[8] and required every buyer or consumer at such a sale to pay this tax to the seller, who in turn was obliged to collect, report and remit this tax to the State.[9] In the years immediately prior to July 1, 1975, the terms "retail sale" or "sale at retail" as used in this statute were defined by RCW Sections 82.08.010 and 82.04.050[10] to include every sale of or charge made for tangible personal property consumed and for labor rendered in the construction of real property by a prime contractor for a consumer. As used in this statute, the term "buyer"

[8] RCW Section 82.08.020, as amended (J.S. App. H-4).

[9] RCW Section 82.08.050, as amended (J.S. App. H-4).

[10] RCW Section 82.08.010, as amended by ch. 244 Laws of 1963, and ch. 149, Ex. Sess., Laws of 1967. RCW Section 82.04.050, as amended (J.S. App. H-1).

was used synonymously with the term "consumer," [11] and the term "consumer" as used in imposing this sales tax was defined prior to July 1975 by RCW Sections 82.08.010 and 82.04.190 [12] as including any person who was the owner or lessee, or had a right to possession of real property which was being improved, altered or constructed. The State likewise levied a use tax [13] upon the privilege of a "consumer['s]" using within the state any article of tangible personal property purchased at retail, or acquired by lease, gift, repossession or bailment with respect to which no Washington sales tax had been paid.[14] The statute imposing the use tax defined the term "consumer" as that term was used in RCW chapters 82.04 and 82.08 with respect to the state's sales tax. The person upon whom the use tax was imposed was responsible for paying it to the State.[15] In addition, the State of Washington authorized cities and counties to levy local sales and use taxes on transactions taxable for state sales and use tax purposes, and occurring within their respective local jurisdictions, collectible in the same manner as the state sales and use taxes.[16]

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[11] RCW Section 82.08.010, *supra*.

[12] RCW Section 82.08.010(3), as amended by ch. 244, Laws of 1963, and ch. 149, Ex. Sess., Laws of 1967. RCW Section 82.04.190, as amended (J.S. App. H-2).

[13] RCW Section 82.12.020, as amended (J.S. App. H-7 - H-8).

[14] RCW Section 82.12.030(2), as amended by ch. 173, Ex. Sess., Laws of 1965, and ch. 149, Ex. Sess., Laws of 1967.

[15] RCW Section 82.12.010 (J.S. App. H-7).

[16] RCW Sections 82.14.030 and 82.14.020, as amended (Mot. to Aff. App. 1a-2a).

Thus, under the statutory scheme prior to July 1, 1975, contractors having prime contracts calling for the improvement, alteration, repair, or construction of real property for private persons, the state government, or the federal government were all treated as sellers and had no state or local sales or use taxes imposed upon them. The private persons and the state government were treated as consumers and had the legal obligation to pay the sales and use tax resulting from construction for them. The United States was also treated as a consumer but was not subject to the state and local sales and use taxes resulting from construction for it because of its immunity from tax under the Supremacy Clause of the United States Constitution.

In order to collect sales and use taxes on construction projects on property owned by the federal government, the State of Washington amended its sales and use statutes by redefining the terms "consumer," "sale at retail," and "retail sale." There is no doubt that the amendments were intended to circumvent the tax immunity of the United States. The legislative history of the 1975 amendments specifically acknowledges that their main purpose was to collect sales and use taxes on federal real property construction projects that previously had been exempt from such taxation (see J.A. 46-59). Thus, specifically excluded from "retail sale" and "sale at retail" were charges for labor and services rendered in the improvement, repair or construction of real property owned by the United States or any of its instrumentalities. Included in those terms were sales of materials to prime contractors engaged in construction work on federally owned real property.[17] The term "consumer" was

[17] RCW Section 82.04.050, as amended by Substitute House Bill No. 86, as enacted into law effective July 1, 1975, as 1975

amended so as to include any person engaged in the business of construction on real property of or for the United States.[18] In addition, the statute was clarified to provide that a use tax would be levied upon a contractor with respect to any material furnished for incorporation into real property construction of or for the United States.[19] This last amendment was enacted to prevent the materials furnished the contractor by the United States for use in construction from escaping tax (J.A. 55-56).

The State admits that by these statutory amendments, it divided prime contractors on real property construction projects into two categories for the purposes of levying and collecting sales and use taxes. The first category consisted of contractors with prime contracts providing for construction on real property owned by private parties, state, and local government agencies The performance of those prime contracts is defined as "retail sales," with the property owners having the duty as "consumers" to pay a sales tax computed on the contract price paid to the prime contractor who has the obligation as a "seller" to collect, report, and remit the collected taxes to the State. The

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Wash. Laws, 1st Ex. Sess., ch. 90, and by Sec. 5 of Substitute Senate Bill No. 2736, enacted into law effective July 2, 1975, as 1975 Wash. Laws, 1st Ex. Sess., ch. 291, Section 5 (J.S. App. H-1; Appellant Br. App. 1a-8a).

[18] RCW Section 82.04.190, as amended by Substitute House Bill No. 86, as enacted into law effective July 1, 1975, as 1975 Wash. Laws, 1st Ex. Sess., ch. 90 (J.S. App. H-2 to H-3; Appellant Br. App. 3a-5a).

[19] RCW Sections 82.12.010 and 82.12.020, as amended by House Bill No. 1229, enacted into law as 1975-1976 Wash. Laws, 2d Ex. Sess., ch. 1 (J.S. App. H-5 to H-8; Appellant Br. App. 8a-12a).

property owner as the consumer is also responsible for paying any use tax on property used in those projects. The second category consists of prime contractors with contracts calling for construction on real property owned by the United States and its instrumentalities.[20] With respect to this second cate-

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[20] This second category also includes prime construction contractors on realty owned by county and city housing authorities. General contractors for city and county housing authorities were first made subject to state sales and use taxation as "consumers" on July 1, 1975, by the very same statutes which the United States is challenging in this case. These public housing authorities have been formed throughout the country pursuant to provisions of and regulations under the United States Housing Act of 1937, 42 U.S.C. 1437 *et seq.*, whereby state and local governments create these agencies to receive federal financing and grants for the purpose of providing low income housing. Federal statutes provide for annual federal contributions to these agencies provided they and their property are exempt from all real and personal property taxes, which include sales taxes levied by state and local governments. 42 U.S.C. 1437d(d). See *Housing Authority of Seattle* v. *Washington*, 629 F.2d 1307 (9th Cir. 1980). The reason that county and city housing authorities' contractors were accorded the same treatment as contractors for the United States is set forth in the legislative history of Substitute House Bill No. 86 dated April 16, 1975. David W. Weig, an economist, there advised Mark McLaughlin of the State's Senate Ways and Means Committee that all housing authority construction in the State of Washington was totally funded by the United States Department of Housing and Urban Development (J.A. 46-48). Thus, it was expected that the sales tax on contractors of such housing authority projects would be passed on to the funding federal agency. It is submitted that this treatment of such housing authority contractors does not lessen the discriminatory nature of the treatment imposed upon the federal contractors.

Contractors constructing roads for federal, city, and local governmental bodies (excluding the state government) are

gory, the prime contractor is defined as the "consumer" with the obligation to pay the sales and use taxes on materials he purchases and uses in the construction project. The effect is that contractors for the United States are required to pay sales and use taxes on material incorporated into federal government construction projects, while other contractors are not required to pay such taxes on materials incorporated into state and private construction projects.

2. The State candidly acknowledges its attempt to circumvent the immunity of the United States not only in its account of the statutory history involved (Br. 4-9) but also in its argument (Br. 11-12). It nevertheless contends that its selective taxation of federal contractors does not violate the tax immunity conferred upon the United States by the Supremacy Clause. In its constricted view of the Supremacy Clause, the State asserts (Br. 30) (emphasis in original) that "[i]t [the Supremacy Clause] does not, in other words, guarantee that the Government can perform a function more cheaply than anyone else. Rather, it protects federal functions from burdens which make the performance of that function *more* costly. *And that is all it does.*" Thus, although the State concedes (Br. 15) that "[a]s a matter of statutory mechanics, federal contractors under Washington law are undeniably treated differently from most other contractors," it asserts (Br. 15-16) that the United States has no ground for complaint unless it is placed at a competitive disadvantage in the marketplace.

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also in this second category and were taxed prior to July 1, 1975, pursuant to RCW Section 82.04.190(3). Historically such road construction projects have received substantial federal financing. See 23 U.S.C. (1952 ed.) 6; 23 U.S.C. (1964 ed.) 103, 106, 107, 120, and subsequent amendments thereto.

But, as we have pointed out (*supra*, pages 18-19), *Moses Lake Homes* establishes that the Supremacy Clause guarantees more than simply that the United States will not be placed at a competitive disadvantage. There, this Court reversed the court of appeals' ruling that would have imposed equal tax burdens on federal and non-federal lessees. The disparities against the federal lessees required the complete invalidation of the state tax against them. Thus, the Supremacy Clause's protection is not merely equivalent to Most-favored Nation status in a tariff treaty. Instead, it absolutely immunizes the contractors and lessees of the United States from any amount of discriminatory state taxation. Indeed, as we have pointed out (*supra*, pages 13-14), "the Court has never questioned the propriety of absolute federal immunity from state taxation." *United States* v. *New Mexico*, *supra*, slip op. 12. Since a tax levied only on federal contractors is equivalent to a tax upon the federal government itself, the Washington tax is barred by the Supremacy Clause.

The fact that the private owners and the State were taxed on construction projects on their property does not, as the State would have it (Br. 34-36), save the Washington tax from invalidity. In *County of Fresno*, this Court emphasized (429 U.S. at 458-459, 463) that the only protection that the United States and those with whom it deals have from abusive state taxation on persons who deal with the United States is the imposition of the tax upon similarly-situated persons. Here, the persons similarly situated are the contractors performing construction for the federal government and the contractors working on privately or state-owned construction projects (see J.S. App. A-11). And it is plain that the contractors who deal with the United States are subject to greater tax bur-

dens than those who deal with the State and with private persons. In these circumstances, as the court of appeals correctly stated (J.S. App. A-13 to A-14 n.14), the necessary political safeguard to protect the contractors who deal with the federal government from abusive taxation would be present only if the contractors who deal with the State and the private sector were similarly taxed. " * * * [I]t does not seem too much to require that the State treat those who deal with the Government as well as it treats those with whom it deals itself." *Phillips Chemical Co.* v. *Dumas School District, supra,* 361 U.S. at 385. See also *Montana* v. *United States,* 440 U.S. 147, 172 (1979) (White, J., dissenting).

Nor can the tax be upheld by regarding it as merely presenting to the United States the choice of reimbursing the contractor for the tax imposed upon him, thereby making him whole, or, in the alternative, refusing to reimburse him so that he bears a burden no other contractor would bear. Indeed, this Hobson's choice confirms the invalidity of the tax. For if the United States reimburses the contractor, it will bear the burden of the state tax. And if it declines to reimburse the contractor, the contractor will be subject to a state tax simply by virtue of its status as a federal contractor. In either event, the discriminatory singling out of the federal government or its contractors for taxation cannot pass muster under the Supremacy Clause.

Contrary to the State's argument (Br. 17-22), this Court has never limited the Supremacy Clause to protecting the federal government from tax burdens which make the performance of its functions more costly. That constricted and novel view of the scope of the immunity doctrine—characterized by the State (Br. 14) as the "no competitive disadvantage prin-

ciple"—draws an invalid distinction between the prohibition against discriminatory taxation of federal contractors with the "absolute federal immunity from state taxation," which "the Court has never questioned." *United States* v. *New Mexico*, *supra*, slip op. 12. Cf. *First Agricultural National Bank* v. *State Tax Commission*, 392 U.S. 339, 350 (1968) (Marshall, J., dissenting). They are one and the same thing for purposes of the Supremacy Clause. At bottom, the discriminatory tax at issue here upon those who deal with the United States is nothing less than a tax on the United States itself. It is therefore barred by the Supremacy Clause.

3. The decisions upon which the State relies do not support its notion that a state can tax the federal government as long as it imposes comparable economic burdens upon the activities of state governments and private parties. In *United States* v. *City of Detroit*, *supra*, 355 U.S. 466, the Court upheld a city tax upon a private party's use for profit of all types of tax-exempt property, including property owned by the United States, on the ground that the tax was not levied on the government and did not discriminate against the government. But in so ruling, the Court reaffirmed (*id.* at 473) that "[i]t still remains true, as it has from the beginning, that a tax may be invalid even though it does not fall directly on the United States if it operates so as to discriminate against the Government and those with whom it deals. Cf. *M'Culloch* v. *Maryland*, 4 Wheat. 316."

Nor does *United States* v. *County of Fresno*, 429 U.S. 452 (1977), support the validity of the Washington tax. As in *City of Detroit*, the Court upheld a state possessory use tax imposed solely on private citizens who use tax-exempt land. Although the plaintiffs were U.S. Forest Service employees, the Court pointed out that the tax did not discriminate against Forest

Service or other federal employees. Indeed, "[t]he Government * * * expressly abandoned its claim, made below [in that case], that the tax treats federal employees who live in federally owned houses differently from state employees who lived in state-owned houses" (*id.* at 464 n.13). *County of Fresno* is therefore distinguishable.[21]

Finally, *United States* v. *Department of Revenue of Illinois*, 371 U.S. 21, aff'g per curiam 202 F. Supp. 757 (N.D. Ill. 1962), upon which the State relies (Br. 23-24), is similarly inapposite. That litigation was initiated by the United States on the ground that the Illinois retailers' occupation tax (sales tax) discriminated against the United States and those with whom it deals because the retailers' occupation tax was imposed upon persons in the State engaged in the business of selling tangible personal property at retail (including those who sold to the federal government), but was not imposed on retailers selling to the State of Illinois and its political subdivisions and to certain charitable organizations. The district court agreed with the United States that as long as the retailers dealing with the State and its political subdivisions were exempt from the occupation tax, the prohibited discrimination was present. *United States* v. *Department of Revenue of Illinois*, 191 F. Supp.

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[21] As the court of appeals correctly pointed out (J.S. App. A-11 to A-12), the Court in *City of Detroit* and *County of Fresno* equated the taxes on the lessees and users of government property with the tax burden upon renters and users of other property, and held that there was no discrimination against them. Here, however, the tax is exclusively laid upon contractors for the United States by virtue of legislation specifically designed to circumvent the immunity of the United States. Hence, there is no comparable tax or tax burden upon contractors for other property owners.

723 (N.D. Ill.), judgment vacated and remanded to consider subsequent events, 368 U.S. 30 (1961), on remand, 202 F. Supp. 757, 758, 760 (1962). On remand, the district court rejected the federal government's argument that the Illinois statute was also discriminatory because it allowed the retailer to pay the occupation tax with the use tax imposed upon private persons. 202 F. Supp. at 760.

Here, the State argues (Br. 23-24) that the Illinois litigation permits a state to tax federal contractors differently from other contractors. But such a reading contradicts the aspect of that decision which held that the tax was nondiscriminatory as long as Illinois imposed it on retailers dealing with the general public, the State, its political subdivisions and the United States. The source from which the retailers received the money to pay the tax was irrelevant to the issue of discrimination.

Moreover, unlike the Illinois litigation, the contractors here who perform construction for the federal government on its land bear a more onerous tax burden than is imposed on contractors doing construction for the State and private persons. It is therefore clear that the Washington tax unconstitutionally discriminates against the United States and those with whom it deals.[22]

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[22] The State also seeks (Br. 37-38) to justify the discrimination against the United States and its contractors involved in this case by reference to decisions involving the taxation of national banks. But the pertinent statute governing state taxation of national banks turns on an entirely different standard from the Supremacy Clause. The bank statute prohibits taxation of national banks "at a greater rate than is assessed upon other moneyed capital in the hands of individual citizens of such State coming into competition with

CONCLUSION

The judgment of the court of appeals should be affirmed.

Respectfully submitted.

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the business of national banks." Rev. Stat. 5219, 12 U.S.C. (1970 ed.) 548. As a result, in determining whether a state tax on state savings and loan shares and national bank shares violates the statute, this Court has taken into account the relative "moneyed capital" controlled by both types of institutions. See *Michigan National Bank* v. *Michigan*, 365 U.S. 467, 477-483 (1961). Accordingly, no persuasive analogy can be drawn from the particularized standard provided by the bank statute.

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Appellants,

v.

UNITED STATES OF AMERICA,
Appellee.

ON APPEAL FROM THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

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I.

Introduction

From a reading of the opening briefs now on file in this case, one underlying question should stand out. That question is as follows:

What is the proper function of the Supremacy Clause of the Federal Constitution—not the Equal Protection Clause but the Supremacy Clause—in a case involving state taxation, not of the federal government, but of those dealing with the government?

This issue is the same whether the parties being taxed are dealing with the Government as lessees from the Government

or as sellers or suppliers to the Government. And it only begs the question to invoke the general principle with which all agree: i.e., that a state tax may not discriminate against the Government or those with whom it deals. Discrimination, after all, is hardly a self-defining term. And this general principle therefore does not tell us what the functional relationship is between the Supremacy Clause and "discrimination" against those with whom the Government deals.

One must, accordingly, further ask: Is the protection afforded those dealing with the federal government by the Supremacy Clause the same as that afforded by the Equal Protection Clause, so that this clause of the original constitution is merely a counterpart of the later adopted 14th Amendment provision? Or is that protection instead derived from, and does it take its content from, the protection afforded by the Supremacy Clause to the Government itself? And if it is the latter *what precisely is it that the Government is protected against?* This, we submit, is the critical question in this case.

Is the protection of the Supremacy Clause in a case such as this a protection to the Government against the imposition of *any* economic incidence or burden of the state tax—just as if the tax were actually imposed, directly, on the federal government itself.[1] Or is the Supremacy Clause at this level, instead, simply a protection to the federal government against being placed at a competitive disadvantage, whether as a lessor or an employer or a purchaser in relation to other lessors, employers or purchasers as the case may be, in the private sector?

We urge, and will further develop in this reply brief, the following answers to the foregoing questions:

(1) The function of the Supremacy Clause, in a case such as this, is to protect the federal government from certain potential effects arising from state taxation of those private parties with whom the government deals, and not to protect those private parties as such—the latter protection being a

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[1]Accord, *McCulloch v. Maryland*, 17 U.S. (4 Wheat) 316 (1819) and its progeny.

function of a different provision in the Constitution—the Equal Protection Clause.

(2) The protection which is afforded to the Government is not, however, a protection against the economic burden of *any* level of state taxation as the appellee here contends and as would be true in the case of a state tax on the federal government itself.

(3) Rather, as illustrated perhaps most graphically by *United States v. County of Fresno*, 429 U.S. 452 (1977), the function of the Supremacy Clause in the context of a state tax on those dealing with the Government is simply to protect the Government from being placed at a competitive disadvantage in relation to those similarly situated lessors, employers, or purchasers, as the case may be, in the private sector or in the public sector at the state and local level. In essence, it thereby eliminates the potential risk that any such competitive disadvantage may be so escalated by a state as to cause a federal function—as lessor, employer, or purchaser—to be impaired.

Or, to state our position in the form of a "black letter" rule:

The Supremacy Clause in the case of a tax on those dealing with the federal government protects the Government against the potential interference with a federal function. That potential interference exists, however, only if the taxing system places the Goverment at a competitive disadvantage when compared to those in the public (state or local) or private sector who are similarly situated to it (i.e., the Government)—as lessors, purchasers, or employers. And to avoid unconstitutionality the class which is "similarly situated" must be sufficiently large to provide a viable political check upon any subsequent increases in the particular tax—whether those increases are through higher rates or an expansion of the tax base.

We have discussed at length in our opening brief the "no competitive disadvantage" test, the "similarly situated" test, and "political check" doctrine; accordingly, we shall avoid

repeating that discussion here. Rather, we will now tie these concepts together, by showing their relationship to each other and, most importantly, their relationship to the Supremacy Clause objective, or goal, of preventing a potential impairment of a federal function.

We will first discuss these relationships, as they have been developed by this Court's decisions, and thereby explain our "black letter" rule. Then, in light of that discussion, we will take up the various arguments of the United States and, thereby, show that they exalt form over substance—and statutory structure over statutory results—in a manner that has already been rejected by this Court. Further, we submit that those arguments, which are couched in terms of "singling out" and "segregation", are thus more appropriate in a race discrimination case under the Equal Protection Clause, actually confuse and obscure *the distinct and different* function of the Supremacy Clause.

II.

The Washington Sales and Use Tax System, as Applied to Federal Contractors, Presents No Risk Of Impairment of a Federal Function.

Our starting point is *McCulloch v. Maryland, supra*, as construed and applied in *Fresno*. The function of the Supremacy Clause, in the context of the factual pattern involved in *Fresno* and that involved here, is to prevent any potential impairment of a federal function. *United States v. County of Fresno*, 429 U.S. at 464. All parties, and the Court below, would accept this common starting point.

This function or objective, however, could be fulfilled in various ways. It could be fulfilled by a rule ("Rule 1") prohibiting any and all taxes on those dealing with the Government, insofar as the tax involves a transaction with the Government. Indeed, at one time this was the rule. *Dobbins v. Commissioner of Erie County*, 41 U.S. (16 Pet.) 435 (1842) (emolument tax on federal officer); *Western Union Telegraph Co. v. Texas*, 105 U.S. 460 (1882) (occupation tax on private corporations). But that approach has since been repudiated by

this Court. See, *e.g., Graves v. New York ex rel. O'Keefe,* 306 U.S. 466 (1939). The Supremacy Clause does not now protect the Government from the possible indirect effect of any and all taxes on those dealing with it.

The function of the Supremacy Clause could also be fulfilled by a rule ("Rule 2") which would be a variation of Rule 1: taxes on those dealing with the Government would be prohibited whenever it could be assumed that the economic burden of those taxes was being passed on to the Government itself. *Panhandle Oil Co. v. Mississippi ex rel. Knox,* 277 U.S. 218 (1928). But that too is not the law. *James v. Dravo Contracting Co.,* 302 U.S. 134 (1937); *Alabama v. King & Boozer,* 314 U.S. 1 (1941); *United States v. New Mexico,* 102 S.Ct. 1373 (1982).

Observe, also, at this point, a common feature of Rules 1 and 2. They are both overbroad—to borrow a term from another area of constitutional law—in that they are broader than necessary to protect the legitimate interests of the federal government. And, correspondingly, if imposed they would thus impede the legitimate interests of the State beyond what should be necessary. For clearly, the legitimate interests of the Government do not require a total freedom from the economic burden of state taxes. See *United States v. Detroit,* 355 U.S. 466, 469 (1958).

Consider next a rule ("Rule 3") which would have been at one time considered the correct one: the legal incidence of a tax may be imposed upon those dealing with the Government (as lessees, sellers, or employees), *only* if the *legal* incidence of that same tax is imposed upon all other lessees, sellers, or employees, as the case may be.

But that is not now the correct rule either. While the taxes involved in such cases as *Graves v. New York ex rel. O'Keefe; Alabama v. King & Boozer,* and *United States v. New Mexico, supra,* would clearly pass constitutional muster under such a rule, the taxes involved in *United States and Olin Mathieson Chemical Corp. v. Department of Revenue of the State of Illinois,* 202 F.Supp. 757 (N.D.Ill. 1962) aff'd per curiam 371 U.S. 21 (1962); *United States v. City of Detroit,* 355 U.S. 466 (1958); and *United States v. County of Fresno,* 429 U.S. 452 (1977) just as clearly would not. Moreover, before

proceeding further let us note the nature of the protection which Rule 3 actually would afford the Government, and precisely how it would do so.

If one assumes that the legal incidence of a tax and its economic burden will always coincide, it follows that the Government would run no risk that its contractors, for example, would be economically burdened by a tax while contractors for other parties are not. The fallacy of this underlying assumption, however, is obvious. The legal incidence of a tax and its economic burden will *not* always coincide, as shown by such cases as *Dravo* and *Alabama v. King & Boozer* (tax shifted from contractor to Government), and *Detroit* and *Fresno* (tax assumed to be shifted from private lessors to private lessees). Moreover, it is often impossible to determine when, and to what extent, such a shift acutally takes place. See *Detroit*, 355 U.S. at 473 n. 4. *Cf. Graves v. New York ex rel. O'Keefe*, 306 U.S. 484-485. The assumption which gives Rule 3 its appeal, then, is often wrong—that we know. What we do not know is precisely when it is wrong.

Lastly, let us consider the rule ("Rule 4") which we submit to be the correct one—as derived from *Olin-Mathieson, Detroit*, and *Fresno*. It is as follows:

In determining the validity of a tax upon a party dealing with the Government in particular transaction, the *legal incidence* of the tax imposed with respect to similar transactions not involving the Government is completely irrelevant. Regardless of which party to such transactions the legal incidence falls upon, the tax on those dealing with the Government is valid so long as the tax on transactions not involving the Government is no lower in rate or base, than the tax imposed with respect to the transaction to which the Government is a party.

For reasons we explained in our opening brief, this is the only rule which is consistent with the results in *Olin-Mathieson, Detroit*, and *Fresno*. (State Br. 22-33) In turn, however, the point to be made here is different, but critical. *The potential risk to the Government under Rule 4 is no different in kind or greater in degree than the potential risk under the Rule 3.* Stated otherwise, the degree and type of

protection afforded the Government by Rule 4 is identical to that afforded by Rule 3. And this is because Rule 3 makes sense under the same assumption as Rule 4, i.e., that in allocating the economic burden of the tax, market forces will not work one way in the private sector, and another way when the Government is involved.

Let us illustrate this point in terms of the tax in issue here: The Washington tax on federal contractors would violate Rule 3, of course, because with respect to non-federal contractors *the legal incidence* of the tax is upon their customers—rather than on the contractors themselves. Once again, however, the most reasonable assumption—if not axiom—is that while the economic burden of a tax may or may not coincide with the legal incidence, market forces will allocate those tax burdens in the same way, whether the Government is involved or not. And under this assumption any technical difference as to legal incidence will make no economic difference at all. Thus the interest of the Government is just as fully protected under Rule 4 as under Rule 3.[2]

While Rule 4 affords the Government no less protection than Rule 3, it affords the States much greater flexibility in fashioning their tax systems; i.e., in determining precisely who is to bear the legal incidence of a particular tax. In other words, to so accommodate the States' interests in making these policy choices involves no greater threat to the Government than does Rule 3.[3] And, hence those interests should be accommodated—just as they were accommodated in

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[2]It is precisely at this point that the Court of Appeals missed the mark in its analysis. The Court was concerned about the possibility that federal contractors might have to bear an economic burden that non-federal contractors did not. (J.S. App. A-12, quoted at U.S. Br. 8) But this possibility, if it exists at all, does not result from, and is not in any way increased by, the fact that technically the legal incidence of the tax is upon the federal contractor. Stated more generally, there is no good reason to assume—as the Court below apparently did assume—that in any transaction the party on whom the legal incidence of a tax technically falls thereby has been automatically deprived of his bargaining power to avoid the economic burden of that tax.

[3]For a further discussion of these policy choices, see the State's opening brief, pp. 18, 19.

Olin-Mathieson, Detroit, and *Fresno.*

This leads us directly back to the question asked at the beginning of this brief. Paraphrased, it asks: what, exactly, is the risk against which the Supremacy Clause protects the Government in the context of a state tax on those with whom it does business? And the answer is that the risk is simply one of an impaired ability to function as a result of being placed in a position of competitive disadvantage with those in the private sector similarly situated. Therefore, if under the State's taxing system the transaction with the Government will produce just one dollar more in tax revenue than a similar transaction not involving the Government, the Supremacy Clause requires that the entire tax must fall.[4] For that one dollar disadvantage could escalate to one million or one billion dollars, with an obvious impairment of a federal function.

The Supremacy Clause, as interpreted by this Court, does not allow a State to take even the first step down this road by imposing a tax on those with whom the Government deals which results in even the first dollar of a competitive disadvantage to the Government. And the "competitive disadvantage" test, in essence, thus here asks: "Has the State of Washington in this case taken that first step?" Clearly it has not.

A final question remains. Does the "no competitive disadvantage" test afford the Government the same scope of protection as does the "political check" test? We believe that it does, and that if properly applied, both tests amount to the same thing. For both focus upon similar transactions, e.g., leases from and purchases by the Government on the one hand and leases from and purchases by other parties on the other. And the criteria for determining which transactions are or are not "similar" should be identical under either test. The difference between the two tests is simply that the "no competitive disadvantage" test emphasizes the reasons why differences in legal incidence should be constitutionally irrelevant in analyzing the discrimination issue under the Supremacy Clause.

A substantive difference, however, would certainly arise if

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[4]Accord, *Moses Lake Homes, Inc. v. Grant County,* 365 U.S. 744 (1961).

narrower criteria for determining "similarity" were applied under the "no-competitive disadvantage" test. This point can be illustrated by the tax involved in *Montana v. United States*, 440 U.S. 147 (1979). That tax was a gross receipts tax applicable only to contractors with public entities, federal, state, and local. As compared with transactions with state and local entities, transactions with the Government suffered from no competitive disadvantage. But as compared with transactions with private entities, they most certainly did. And for this same reason, "* * * the 'political check' that would have been provided by private sector contractors 'against abuse of the taxing power [is] lacking' ". *Montana v. United States*, 440 U.S. at 168 (Justice White dissenting).

With that we turn to the submission of the United States to see what, if any, answer it provides to the questions we have just addressed.

III.

The United States Misconceives the Scope of the Protection Afforded the Government by the Supremacy Clause.

The United States has twice asserted in its brief that "* * * the Supremacy Clause guarantees more than simply that the United States will not be placed at a competitive disadvantage." (U. S. Br. 11,27) Significantly, however, the United States nowhere asserts that Washington's tax *does* place the Government at a competitive disadvantage. Nor does it deny that striking down the tax would, indeed, place the Government at a competitive *advantage*.

But what, then, is the "more" that the Supremacy Clause guarantees? "* * * [I]t absolutely immunizes the contractors and lessees of the United States from any amount of discriminatory state taxation." (U. S. Br. 27) The United States, however, nowhere clearly explains its criteria for determining what constitutes a "discriminatory" tax; i.e., a tax which for some reason remains "discriminatory" even though it does not place the Government at any competitive disadvantage and even though its elimination would afford the

Government a clear competitive advantage.

There are, however, two themes which run throughout the United States's brief and which may embody its proposed criteria for a discriminatory tax. The first theme is cast in terms that would be more appropriate in a racial discrimination case arising under the Equal Protection Clause. Under Washington's tax system, it is asserted, Government contractors "are singled out for a special tax. * * *" (U. S. Br. 14; see also U. S. Br. 11,16). And indeed, these contractors are made subject to a type of "segregation". (U. S. Br. 10, 15). This theme will be examined in the next section of this brief, in which we discuss three principal cases which are relied upon by the United States and which, it is asserted, prohibit such "singling out" or "segregation". We simply suggest here that it only confuses the issues and impedes analysis of the constitutional interests involved to cast the discussion in such terms.

The second theme, though related to the first, is more substantive and might be called the "circumvention" theme. Its clearest articulation is found in the following passage:

> "The United States, like other entities, can act only through those who serve it in one capacity or another. Its immunity would mean little if, whenever a state law of general applicability had its legal incidence upon the United States, the State could then turn and enact parallel special legislation directed only to those who serve or deal with the United States. Cf. *United States v. Mississippi Tax Commission*, 412 U.S. 363 (1973); *United States v. Mississippi Tax Commission*, 421 U.S. 599 (1975). To single out for taxation those who serve the United States is to tax the United States itself." (U. S. Br. 21. See also, U. S. Br. 12, 14, 15).

The last sentence of this statement, however, only confuses things once again. The prohibition of the Supremacy Clause against discriminatory state taxes, with which we are here concerned, and its companion prohibition against any direct taxes upon the United States (even if they be non-discriminatory) derive from completely different policy considerations. The former prohibition is based upon the need to prevent any potential impairment of a federal function through abusive state taxation. *United States v. County of*

Fresno, 429 U.S. at 458-459. The principal purpose of the latter prohibition, on the other hand, is "* * * that of forestalling 'clashing sovereignty', *McCulloch v. Maryland*, 4 Wheat. at 430, by preventing the states from laying demands directly on the Federal Government", *United States v. New Mexico*, 102 S.Ct. at 1382-83.

We do not necessarily disagree with the thrust of the second sentence quoted above. Rather, it is the conclusion which the United States attempts to draw from that statement which does not follow. As this Court has pointed out in *United States v. New Mexico*, even the immunity of the United States from direct taxes no longer means very much; indeed, the Court quite correctly characterized it as having "essentially symbolic importance" (*United States v. New Mexico*, 102 S.Ct. at 1383). And, in turn, the taxes upheld in *Olin Mathieson*, *Detroit*, and *Fresno* certainly had the effect of circumventing the immunity of the Government from direct taxation—and leaving that immunity with little economic meaning and only "symbolic importance". By the same token, the tax challenged here does no more.

Further, it will be seen that even the tax upheld in *New Mexico*, which beyond question was non-discriminatory, had the effect of circumventing the immunity of the Government. If, for example, the Government had refused to reimburse the contractors in New Mexico for the four percent State gross receipts tax while other contractors were able to avoid the economic burden by passing that tax on to their customers, the result clearly would have been to place the federal contractors at an economic disadvantage, and to that extent discriminate against them. The Government could remove this discrimination or disadvantage only by giving up the economic benefit of its own tax immunity, through reimbursing its contractors for their taxes. Thus, the only way to avoid the circumvention of which the United States here complains would be to go back to what we have here described as Rule 1 or Rule 2. (See p. 4-5, *supra*). Rule 3 no more prevents this circumvention than does Rule 4. (See pp. 6-7, *supra*).[5]

[5]And this is the short answer to the United State's suggestion that we would present the Government with a Hobson's choice. (U. S. Br. 28).

We next turn, then, to the "singling out" and "segregation" theme, and an examination of the principal cases on which the United States relies.

IV.

The Principal Cases Relied Upon by the Government do Not Show That the Washington Tax is Unconstitutionally Discriminatory Under The Supremacy Clause.

Each party to this controversy relies principally upon a trilogy of cases. The Government's trilogy is *Miller v. Milwaukee*, 272 U.S. 713 (1927); *Phillips Chemical Co. v. Dumas School District*, 361 U.S. 376 (1960); *Moses Lake Homes, Inc. v. Grant County*, 365 U.S. 744 (1961).[6] These three cases, it is asserted, bar "* * * a state from singling out those who deal with the United States for special tax burdens". (U. S. Br. 16). Before discussing the Government's cases however, it may be helpful to recall precisely how federal contractors came to be "singled out", and just how "special" the tax burden imposed upon them actually is—and is not.

When the Washington sales and use tax was first adopted in 1935, not only were all prime contractors (without exception) taxed alike, but all other persons who purchased personal property for their own use were taxed in the same manner as all prime contractors. And construction materials, by whomever purchased, were taxed in the same manner as cars, furniture, food, or other personal property.

This uniform pattern was then altered in 1941. All prime contractors were singled out for special treatment.[7] They were made sellers rather than buyers, and the taxable transaction

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[6]Our trilogy is, of course, *United States v. City of Detroit*, 355 U.S. 466 (1958), *United States and Olin Mathieson Chemical Corp. v. Illinois Department of Revenue*, 371 U.S. 21 (1962) and *United States v. County of Fresno*, 429 U.S. 452 (1977).

[7]Most states continue to tax contractors in the same way as Washington taxed them before 1941; *i.e.*, they are buyers rather than sellers. See, CCH, State Tax Case Reporter, All States, p. 6047. Similarly, Washington has also treated as "buyers" contractors identified as "speculative builders," *i.e.*, those constructing buildings for sale or rental upon land owned by such contractors but without any pre-determined vendee or lessee under contract or lease. Washington Administrative Code § 458-20-170.

was thus changed from the sale of the tangible personal property to the contractor to the contractor's total job for his customer—which included the cost of labor and the amount of any profit, as well as the cost of materials.

In turn, the 1975 amendments under challenge in this case made a further exception to the previous, 1941, exception to the original, 1935, uniform pattern. In essence, federal contractors were put right back where they were before, from 1935 to 1941. Once again, they were treated the same as purchasers of cars, furniture, food, or other personal property for their own use.

Thus the Government's assertion that federal contractors were "singled out" by the 1975 amendments rests more upon semantics than substance. If the earlier 1941 change had been so tailored as to apply only to *non-federal* construction while leaving federal construction in the exact same tax status as before, who is it that would have been "singled out"? Federal contractors? Or non-federal contractors? We would suggest the latter. But regardless of how that semantic debate might be resolved, the debate should be of no constitutional significance. For the substance of the amendments under challenge was to do no more, in 1975, than might have been done in 1941, in the manner just described.

There is, however, a second aspect to this "singling out" issue which is indeed one of substance rather than semantics. During the period from 1941 to 1975, transactions involving construction for the Government actually enjoyed a preferred status. At no stage in the process was a sales or use tax imposed on either the materials purchased by the contractors or on contractors' labor or profit. The 1975 amendments removed that preference.

Thus, the 1975 amendments are actually quite similar to those involved in *Macallen Co. v. Massachusetts*, 279 U.S. 620 (1929) which the Court described as follows in *Pacific Co. v. Johnson*, 285 U.S. 480 (1932) at 494:

> "* * * 'There the Commonwealth, which had long imposed a tax on corporate franchises measured by taxable income of the corporation, amended its statutes so as to add the income from tax-exempt bonds of the federal government to the measure of the tax. It was held

> that this change of taxation policy, embodied in the statute and "adopted as though it had been so declared in precise words for the very purpose of subjecting these securities pro tanto to the burden of the tax," was invalid. *Thus the legislative abandonment of a policy which had previously discriminated in favor of tax-exempt securities was treated as a discrimination against them, and the tax, although in fact non-discriminatory, was condemned as analogous to the discriminatory tax held invalid in the Miller Case* [Miller v. Milwaukee, 272 U.S. 713, * * *].'" (Emphasis supplied.)

The Government would have this Court do here something very similar to what it did in *Macallen*: It would have the Court treat Washington's abandonment of a policy, which had previously discriminated *in favor of* federal construction projects, as a discrimination *against* such construction projects. But *Macallen*, of course, no longer has precedential value. See, *Phillips Chemical Co. v. Dumas School District*, 361 U.S. 376, at 382, *United States v. Detroit*, 355 U.S. 466, at 472, note 2. Its long since discredited approach, therefore, should not be revived here.

1. *Miller.*

We turn, then, directly to *Miller v. Milwaukee*, 272 U.S. 713 (1927). The Government appears to argue that, in *Phillips*, the *Miller* decision was reaffirmed and applied in all its pristine vigor. (See, U. S. Br. 17). In fact, just the opposite is true.

> "Phillips argues that because Article 5248 applies only to private users of federal property, it is invalid for that reason, without more. For this argument, it relies on Miller v Milwaukee, 272 US 713, * * *; see also Macallen Co. v Massachusetts, 279 US 620." *Phillips*, 361 U.S. at 382.

Phillips was arguing that Article 5248 was a rifle shot aimed solely at federal lessees—which is exactly what it was. Accordingly, the argument went, that statute was invalid under *Macallen* and *Miller*. There was no need to examine any other portion of the Texas property tax structure. The Court in *Phillips*, however, *rejected* this argument, and thereby limited *Miller* in a manner that is directly relevant here.

After discussing *Miller* and *Macallen*, the court concluded:

> Thus, if Miller has any relevance here, it is only to the extent that is may support the proposition that a State may not single out those who deal with the Government in one capacity or another, for a tax burden not imposed on others similarly situated.
>
> "A determination that Article 5248 is invalid, under this test, cannot rest merely on an examination of that article. It does not operate in a vacuum. First, it is necessary to determine how other taxpayers similarly situated are treated. Such a determination requires 'an examination of the whole tax structure of the state.' Cf. Tradesmens Nat. Bank v Oklahoma Tax Com. 309 US 560, 568, 84 L ed 947, 952, 60 S Ct 688. Although Macallen may have departed somewhat from this rule, nothing in Miller, at least as it has been interpreted in later cases, should be read as indicating that less is required." (Emphasis supplied. 361 US at 382, 383).

As applied in *Phillips*, then, *Miller* established no more than the general principle of non-discrimination. Precisely how that principle is to be applied in this case, however, is shown by our trilogy of cases, *Detroit*, *Olin Mathieson*, and *Fresno*—to which we will add *Phillips* itself. These cases provide the ending point: *Miller* provides only the starting point.

2. *Phillips.*

The second part of the Government's trilogy, *Phillips Chemical Co. v. Dumas School District, supra*, not only fails to support the Government's position, but actually supports ours. As we have just seen, *Phillips* establishes that even a statutory rifle shot aimed only at those dealing with the Government is not, ipso facto, discriminatory. One must examine the whole tax structure of the State, to see who else is or is not shot at, before determining whether that statute is discriminatory.

Phillips did, of course, strike down the tax imposed by Article 5248 of the Texas statutes on federal lessees. But even this holding does not support the argument of the United States here.

In *Phillips*, a tax was imposed upon lessees of real property owned by the Government, measured by the full value of the fee, whereas under similar leases with the state and its political subdivisions as lessors, no tax was imposed at all—on either lessor or lessee.

Phillips would be dispositive, we agree, if construction for the state and its political subdivisions were completely exempt from any sales or use tax. But such construction is not so exempt. Indeed, construction for the state and its political subdivisions bears a higher tax burden than construction for the Government, not a lesser burden.

But there is more to *Phillips* than this. Under *Phillips*, a tax on the non-federal lessor serves just as well, constitutionally, as a tax on the lessee;[8] and so too here, a tax on the non-federal customer of the contractor serves just as well as a tax upon the contractor himself. The legal incidence of the tax, in short, is irrelevant. *Phillips* thus supports the adoption of our Rule 4, *supra*, rather than Rule 3.

3. *Moses Lake Homes.*

Moses Lake Homes v. Grant County, 365 U.S. 744, involved two issues, one substantive and the other procedural or remedial. Under Washington law for determining the assessed value of leaseholds on real property owned by the state and its political subdivisions, the assessed value was not the value of the fee itself, but rather the value of the leasehold interest, which was usually substantially less than fee value and in fact often zero. (See, *Moses Lake Homes*, 365 U.S. 744, at 750, and the Washington cases cited therein.) But the County claimed that it could value improvements owned by the Government and leased to a private corporation at full fee value of the improvements. In response to that contention, and the first issue, this Court held that such a claim could not

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[8]The imposition of the property tax on private *lessors*, including charities, churches and similar entities which lease their property to a business lessee, led the Court to conclude:

"Under these circumstances, there appears to be no discrimination between the Government's lessees and lessees of private property." 361 U.S. at 381.

See also footnote 6, 361 U.S. at 381.

be sustained in the face of *Phillips*. 365 U.S. at 752. That aspect of the case, accordingly, does not support the Government any more than does *Phillips*.

As for the second issue in *Moses Lake*, it is likewise not in point. There, the County's tax claim had worked its way through the federal court system by reason of a condemnation action initiated by the United States in Federal District Court, to acquire the leasehold interest, and thereby eliminate it. The District Court upheld the valuation method used by the County in its tax claim. The Court of Appeals, however, found that method discriminatory. But instead of invalidating the whole tax claim, the Court of Appeals remanded the case with directions to the District Court to adjust the claim on the basis of a non-discriminatory method of valuation. In this, the Court of Appeals erred. See 365 U.S. at 752.

We are not, however, asking this court to do what the District Court was improperly directed to do in *Moses Lake Homes*. We are not asking for the rewriting or revision of a tax claim, a tax statute, or anything else. We are only asking the Court to determine whether a tax statute "is or is not a valid one." 365 U.S. at 752. *Moses Lake Homes* is thus not in point.

V.

Olin Mathieson, Detroit, and Fresno are not Distinguishable.

The United States begins its efforts to distinguish our trilogy of decisions by stating:

> "The decisions upon which the State relies do not support its notion that a state can tax the federal government so long as it imposes comparable economic burdens upon the activities of state governments and private parties." (U.S. Br. 29)

That is not our "notion" or contention at all. In accusing the State of taxing the Government, the United States is attempting to meld into one the two distinct pronibitions of the Supremacy Clause. (See pp. 10-11, *supra*).

The United States attempts to distinguish *Detroit* simply by noting a fact with which we do not disagree at all: *Detroit*

reaffirmed the constitutional principle that a state tax may not discriminate against the Government or those with whom it deals. (U.S. Br. 29). The United States does not attempt to explain, however, why the tax in *Detroit* did not violate that principle, while the similar tax in this case does, or why the tax in this case should be considered as dissimilar from that in *Detroit* in applying that principle.

The attempt to distinguish *Fresno* is likewise wide of the mark. The United States points out that in *Fresno* it had abandoned its claim that the California tax treated federal employees living in federally owned housing differently from state employees living in state-owned housing. (U.S. Br. 30). That, however, was hardly the decisive factor in *Fresno*. The decisive factor was that the California property tax was also generally imposed upon *private* lessors, who, the Court then assumed, passed the tax on to their lessees. The tax on state employees would hardly have preserved the California tax on federal employees from the charge of discrimination, for the very reasons spelled out in Justice White's dissent in *Montana v. United States*, 440 U.S. 147, at 170-171. What saved the tax was the similar tax on private lessors.

The United States acknowledges as much in footnote 21 (U.S. Br. 30), and there tries to bolster its effort to distinguish *Detroit* and *Fresno*. The Government there recognizes the equation between *taxes* on lessees (the possessory interest tax) and *"tax burdens"* on other lessees (the real property tax on lessors which both *Fresno* and *Detroit* say can be presumed to have been passed on to lessees). Then, at the conclusion of the footnote the Government states that in this case there is "no comparable tax *or tax burden* upon contractors for other property owners." But this statement reflects nothing more than an assumption on the Government's part that non-federal property owners will in all circumstances bear the economic burden as well as the legal incidence of the tax.[9] This assumption is no more warranted than an assumption that the private lessors in *Detroit* and *Fresno* would in all circumstances have borne the economic burden, as well as the

[9]It is essentially the same as the assumption which gives surface appeal to what we have called Rule 3. See pp. 5-6, *supra*.

legal incidence, of the property tax. And this Court, in turn, made exactly the opposite assumption.

The most tenable assumption of all, we submit, is that if market forces warrant the federal contractor bearing the economic burden, his non-federal counterparts will, as a result of those same market forces, be faced with the same economic burden in the private or public (state and local) sectors. And conversely if the non-federal contractor can avoid that economic burden, so can his federal counterpart. (See p. 6, *supra*.)

And under this assumption, the central concern of the Court in both *Detroit* and *Fresno* is met; equality of economic burdens between those dealing with the Government and their counterparts in the private or public sectors. And however one phrases the applicable test to determine discrimination, be it the similarly situated test, the political check test, or the "no competitive disadvantage" test, there simply is no discrimination. All applicable tests are met.[10]

Conclusion

In addition to an absolute immunity from direct taxation, the Supremacy Clause affords the Government a limited protection from the economic burden of a state tax on those with whom it does business. But it does not insure the Government a competitive advantage over others engaged in similar activities. Rather, it simply protects the Government against potential impairment of its functions by being placed in a position of competitive disadvantage. And it is possible for that protection to be achieved by various rules or postulates, including a total ban on any state taxation of federal contractors or the like, or a rule allowing the states to tax those dealing with the Government only where the legal incidence of the same tax is imposed on all others similarly situated. Precisely the same protection, however, is afforded the Government under an alternative rule, under which the legal incidence of the tax as applied to non-federal

[10]The United States' discussion of *Olin Mathieson* (U.S. Br. 30,31) is almost word-for-word the same as its discussion of this case in its Motion to Affirm (Motion 9-11). Our opening brief (State Br. 23,24) fully answers both.

transactions is irrelevant. It only requires that the economic burden of the tax—however it be actually allocated in any given case—can be no greater when the Government is involved than when it is not. Yet this latter rule, which we here advocate and which, we submit, is implicit in the trilogy of already decided cases (*Detroit*, *Fresno* and *Olin-Mathieson*) on which we rely, has the added virtue of also allowing the states the greatest degree of flexibility in fashioning their tax systems. Properly analyzed, those three cases can only be adequately explained on the basis of such a rule—but under that rule all three were correctly decided. In turn, under the same rule, the lower court's decision in this case was in error and should be reversed.

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IN THE SUPREME COURT OF THE UNITED STATES
October Term, 1981

STATE OF WASHINGTON, DEPARTMENT OF REVENUE OF THE STATE OF WASHINGTON, AND CHARLES W. HODDE, Director of Revenue, and His Successors in Office,

Appellants,

v.

UNITED STATES OF AMERICA,

Appellee.

ON APPEAL FROM THE UNITED STATES COURT OF APPEALS, NINTH CIRCUIT

BRIEF ON BEHALF ON STATE OF CALIFORNIA AS AMICUS CURIAE IN SUPPORT OF APPELLANT

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QUESTIONS PRESENTED

Does the Supremacy Clause of the Federal Constitution prohibit a state from imposing a sales or use tax upon a private builder doing business with the federal government under the following circumstances:

(a) All other private builders engaged in a similar business with all other persons, including the state, its agencies and local governments, must pay a sales tax measured by the total contract price, but have the right and obligation under state law to collect that tax as reimbursement from those with whom it is doing business;

(b) Builders doing business with the federal government, on the other hand, have no such right or obligation under state law, but instead must look to the provisions of their contract with the federal government for any reimbursement of the taxes they pay?

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No. 81-969

IN THE SUPREME COURT OF THE UNITED STATES

October Term, 1981

STATE OF WASHINGTON, DEPARTMENT OF REVENUE OF THE STATE OF WASHINGTON, AND CHARLES W. HODDE, Director of Revenue, and His Successors in Office,

Appellants,

v.

UNITED STATES OF AMERICA,

Appellee.

ON APPEAL FROM THE UNITED STATES COURT OF APPEALS, NINTH CIRCUIT

INTEREST OF AMICUS CURIAE

The State of California is now defending two lawsuits in federal courts wherein the United States District Court on July 12, 1982,[1] ruled that the California

1. U.S.A. v. Cal. St. Board of Equalization, U.S.D.C., Central District of California, No. 79-03359-R; U.S.A. v. Calif. St. Board of Equalization, U.S.D.C., Central District of California, No. 81-1588-R.

sales tax is unconstitutionally discriminatory as applied to gross receipts of retailers selling or leasing to the United States and its instrumentalities.

In addition, a federal court appeal is now pending wherein it is asserted that the Court of Appeal's decision below in this case prevents California's collection of tax under its Sale and Use Tax Law with respect to sales of materials and fixtures to United States contractors. (Edward W. W. Howell, etc., debtor (U.S.D.C. No. Dist.) Cal. #81-4504-SW.)

* * *

(footnote 1 cont'd)

The same judge has earlier made the same ruling, but the Court of Appeals (9th Cir.) and this Court on earlier appeals did not rule on the discrimination questions. (See 650 F.2d 1127; #81-1000.)

SUMMARY OF ARGUMENT

Washington imposes a sales tax on consumers who purchase contractors' services. Where the consumer is immune from tax, Washington imposes a (lighter) tax on the contractor. This is an example of a "complementary" tax system under which a second tax is placed on a different party to a single transaction, to insure collection of a tax when the party to the transaction normally taxed is immune or exempt from taxation (e.g., seller-purchaser and lessor-lessee). This Court has, several times, and we believe uniformly, held such complementary taxes not to be unconstitutionally discriminatory, apparently on the basis that it makes no difference which party to the transaction is taxed because they are free to shift the tax burdens through their contractual arrangements.

The court below, we believe, misinterpreted and improperly distinguished this Court's earlier rulings. The distinctions made by the Ninth Circuit below make no sense and would render this Court's earlier decisions meaningless. This Court should rule that Washington's tax on contractors is not unconstitutionally discriminatory.

* * *

ARGUMENT

I

THIS COURT HAS CONSISTENTLY HELD THAT COMPLEMENTARY TAXES ON DIFFERENT PARTIES TO A TRANSACTION ARE NOT UNCONSTITUTIONALLY DISCRIMINATORY WHERE THE PARTIES CAN CONTRACTUALLY SHIFT THE TAX BURDEN AMONG THEMSELVES

This Court has upheld (we believe consistently) a number of "complementary" taxes designed to prevent escape from taxation of transactions where the party normally taxed is immune or exempt from taxation, against the claim that such taxes are unconstitutionally discriminatory. The rule would appear to be that even though a tax is imposed upon different taxpayers, no unconstitutional discrimination exists where the tax burden can be equalized through the normal contracting arrangements between the parties subjected to the different taxes.

A. A Sales or Use Tax May Be Constitutionally Imposed on a Purchaser or Seller Where the Other is Immune From the Normally Imposed Tax

In Southern Pac. Co. v. Gallagher (1939) 306 U.S. 167, this Court directly rejected the proposition that imposing a different but equal tax on the different parties to a single transaction created unconstitutional discrimination, stating,

> "A discrimination against goods of out-of-state origin on the face of the sales and use acts is suggested because the local retailer may absorb the sales tax while the consumer of an imported article must pay the use tax. But this is not a discrimination in the law. California's exaction for the distribution of tangible personal property is the same, whether purchased within or without her borders or whether paid by the retailer or consumer." (Id., at p. 172.)

Under either the sales or use tax considered in Gallagher a single tax (an equal amount) must be paid arising from the sale of tangible personal property

for use in California. The seller must pay the sales tax and has no legal right to collect it from the buyer; he must take this into consideration in negotiating the sale contract. The use tax is the legal obligation of the buyer, and can be collected from him separate from any sales price; he must take this into consideration in negotiating his sales price. Ability of a buyer and seller to balance the sales and use tax obligations in the contractual process obviates any discrimination which might otherwise invalidate the imposition of a sales tax on some transactions and the use tax on others where the seller is immune from tax.

In the Gallagher case the primary tax was sales tax and the "pick-up" tax or complemental tax was the use tax. A converse situation was present in United States v. Dept. of Revenue of

Illinois (Olin Mathieson) (1962) 371 U.S. 21, where this Court affirmed, per curiam a three-judge district court decision appearing in 202 F.Supp. 757. The Olin Mathieson three-judge court stated:

> "Plaintiffs' argument on discrimination concedes that the use tax is not exacted from the federal government and it is urged by plaintiffs that a retailer who sells to the federal government must pay the occupation tax out of his own pocket because he cannot collect the use tax from the purchasing sovereign; whereas a retailer dealing with a purchaser who is not the federal government need not pay the occupation tax when he collects the use tax from such purchaser. This contention of 'discrimination' among retailers because of the immunity of the United States from taxation contradicts the theory urged by plaintiffs. A discrimination among taxpayers resulting from adherence to the doctrine of severeign immunity is not only reasonable but mandatory." (United States v. Dept. of Revenue, State of Ill., supra, 202 F.Supp. at p. 760.)

It is believed that the Olin Mathieson decision is in point. This Court should here rule that a tax on a seller (contractor) is not unconstitutionally discriminatory where the normal or regular tax is normally placed instead on the purchaser-user.

B. Similarly, a Tax May Be Imposed on a Lessor or Lessee Where the Usual Tax is Imposed on the Other Party Who is Tax Immune

In United States v. Detroit (1958) 355 U.S. 466, this Court upheld a tax on a lessee of property belonging to the United States against the charge that this tax discriminated because the normal or usual tax was a property tax on owners, not on lessees. This Court there held:

> "It still remains true, as it has from the beginning, that a tax may be invalid even though it does not fall directly on the United States if it operates so as to discriminate against the Government or those with whom it deals. [Citation.] But here the tax applies to

every private party who uses exempt property in Michigan in connection with a business conducted for private gain. Under Mighigan law this means persons who use property owned by the Federal Government, the State, its political subdivisions, churches, charitable organizations and a great host of other entities. The class defined is not an arbitrary or invidiously discriminatory one. As suggested before the legislature apparently was trying to equate the tax burden imposed on private enterprise using exempt property with that carried by similar businesses using taxed property. Those using exempt property are required to pay no greater tax than that placed on private owners or passed on by them to their business lessees. In the absence of such equalization the lessees of tax-exempt property might well be given a distinct economic preference over their neighboring competitors, as well as escaping their fair share of local tax responsibility. [Citation.] Nor is there any showing that the tax is in fact administered to discriminate against those using federal property. To the contrary undisputed evidence introduced by appellees demonstrates that lessees of other exempt property have also been taxed." (U.S. v. Detroit, supra, at pp. 473-474.)

In 1977, this Court upheld in United States v. County of Fresno 429 U.S. 452, a "possessory interest" tax on lessees of residences belonging to the United States where the property owner-lessor could not be subjected to the normal property tax. At that time, this Court stated:

> "Although the tax is imposed by the appellee counties on renters of real property only if the owner is exempt from taxation--and consequently is not imposed on the vast majority of renters of real property in California--the tax is not for that reason discriminatory. In this respect this case is governed by United States v. City of Detroit, 355 US 466. There the city of Detroit imposed a use tax on those who used tax-exempt property owned by the United States.
>
> "The tax was measured by the value of the property. With respect to nonexempt property, a similar tax was imposed on the owner and none on the user. In answering an argument that the tax discriminated against those dealing with the Federal Government, the Court said:
>
> 'As suggested before the legislature apparently was trying to equate the tax

> burden imposed on private enterprise using exempt property with that carried by similar businesses using taxed property. Those using exempt property are required to pay no greater tax than that placed on private owners or passed on by them to their business lessees.' Id., at 473-474, Emphasis added.)
>
> Similarly, here the State of California imposes a property tax on owners of nonexempt property which is 'passed on by them them to their . . . lessees.' Consequently, the appellants who rent from the Forest Service are not worse off under California tax laws than those who work for private employers and rent houses in the private sector." (U.S. v. County of Fresno, supra, at pp. 464-465.)

In these leasing-possessory interest cases, the ability of the contracting parties to adjust their property rental arrangements again obviates any discrimination which might otherwise result from placing the tax obligation on different persons where the normal taxpayer is immune from tax. The same reasoning and result should obtain where the usual tax

is on the lessee and the lessor is taxed only when the lessee is immune. (This situation exists in the two pending cases cited in footnote 1, supra.)

It is respectfully submitted that the foregoing cases clearly establish the rule of this Court that where a party to a lease or sale transaction normally taxed is immune from taxation, a state may impose a complemental or pick-up tax on the other party to the transaction without violating constitutional prohibitions against discrimination.

* * *

II

THE OPINION OF THE COURT OF APPEALS BELOW MISCONSTRUED AND EVISCERATED THE DECISIONS OF THIS COURT, AND SHOULD BE REVERSED

The Court of Appeals below not only totally ignored the Gallagher and "Olin Mathieson" cases discussed above, but misconstrued the holdings of this Court in the Fresno and Detroit cases quoted herein above. The court below seems to limit validity of a complementary tax to those situations where the persons taxed "necessarily have another's tax burden economically shifted to them, as occurred in Fresno and Detroit."(654 F.2d at 576, also fn. 12.) While admitting that the state taxing method "might have the effect of forcing the federal government to reimburse the contractors for the amount of tax that they must pay,to the state" (Id., at p. 577), the court below said the record does not establish that "the

economic incidence of the sales and use tax would necessarily be shifted" to the contractors. (Id., at p. 576, see fn. 12.) It would establish the requirement of proof that the economic incidence must necessarily be passed on in order to avoid discrimination. Such statement clearly misconstrues the opinions of this Court.[2/] It is respectfully submitted that the economic opportunity of contracting parties to adjust and balance the economic burden

2. The Ninth Circuit held in U.S.A. v. Cal. Bd of Equalization (1981) 650 F.2d 1127 (affirmed without opinion March 29, 1982, #81-1000) that economically requiring a tax be passed on shifts the legal incidence to the consumer. Thus, the Ninth Circuit would place the states in a "Catch-22" position of requiring the burden to be passed on to avoid constitutional discrimination, but elsewhere finding that requiring the burden to be passed on shifts the legal incidence and creates unconstitutional taxation of the federal government as purchaser-lessee. However, the Detroit and Fresno cases held that the legal incidence was not passed on, making it clear that unconstitutional discrimination is avoided where the opportunity exists, not only where the necessity exists.

of a tax is all that is necessary to avoid unconstitutional discrimination in imposing a tax on one or the other of the contracting parties. We find nothing in the Fresno, Detroit, Gallagher, or Olin Mathieson cases which suggest that there was any necessity that the burden of the tax be passed from seller or lessor to the purchaser or lessee. The approach taken by the court below would appear to effectively preclude any kind of complementary tax system because the parties, through their freedom to contract, could assure that there was no "necessity" that the tax be passed on.

The custom and practice of all businessmen is to recover all of their costs and a profit - including all the tax that they must pay from their purchasers or lessees. No contractor in this case is going to fail to pass on his tax costs

any more than a property owner leasing real or personal property being discussed in the Detroit and Fresno cases would do so. The contractors in this case clearly could pass on their tax costs as part of their contract price or by contracting for tax reimbursement -- they were not discriminated against. The fact that their right to pass on tax burden is contractual while those of other contractors is statutory, does not create unconstitutional discrimination.

CONCLUSION

This Court has recognized that those who do business with the government must pay their fair share of taxes. To prevent the use of complementary taxes -- applied to another party to a transaction where the normal taxpayer is exempt -- would allow transactions involving the federal government to completely avoid the tax

while all of the similar transactions pay their part of the cost of government. Millions of dollars of state revenue are involved. The burden of a tax can be divided or passed between sellers and purchasers and between lessors and lessees by contractual arrangements between the parties. This Court has specifically ruled in the Gallagher, Olin Mathieson, Detroit, and Fresno cases that this contractual ability to pass on or redistribute the tax burden eliminates unconstitutional discrimination under the circumstances

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before this Court. The Olin Mathieson ruling is in point, this result should be made clear in this case, and the Ninth Circuit should be reversed.

Respectfully submitted,

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Docket Sheet

NO. 81-969-AFX	TITLE Washington, et al., Appellants v. United States

DOCKETED	COURT
Nov. 20, 1981	United States Court of Appeals for the Ninth Circuit

DATE	PROCEEDINGS AND ORDERS
	Counsel for Appellants: Timothy R. Malone
	Counsel for Appellee: Solicitor General
Nov. 20, 1981	Statement as to jurisdiction filed. (RECORD FILE).
Dec. 18, 1981	Order extending time to file a resqponse to the petition until Jan. 22, 1982.
Jan. 26, 1982	Motion to affirm filed.
Jan. 25, 1982	Brief, amicus curiae, on Behalf of the State of California filed.
Jan. 27, 1982	DISTRIBUTED. 2-19.
Feb. 2, 1982	Motion of Multistate Tax Commission for leave to file a brief as amicus curiae filed.
Feb. 3, 1982	DISTRIBUTED. 2-19. (Above motion)
Feb. 19, 1982	Reply brief for the appellants filed. (D).
Feb. 22, 1982	The motion of Multistate Tax Commission for leave to file a brief as amicus curiae is GRANTED.
Mar. 23, 1982	DISTRIBUTED. 3-26.
Mar. 30, 1982	REDISTRIBUTED. 4-2.
Apr. 1, 1982	Supplemental brief in opposition to motion to affirm filed.(D)
Apr. 13, 1982	REDISTRIBUTED. 4-16.
Apr. 20, 1982	REDISTRIBUTED. 4-23.
Apr. 27, 1982	REDISTRIBUTED. 4-30.
May 10, 1982	REDISTRIBUTED. 5-13.
May 17, 1982	Probable jurisdiction NOTED.

June 24, 1982	Order extending time to file the joint appendix and appellants' brief on the merits until July 21, 1982.
July 23, 1982	Brief, amicus curiae, of the State of California in support of appellant filed.
July 24, 1982	Joint appendix filed.
July 24, 1982	Brief for the appellants filed.
Aug. 20, 1982	Order extending time to file the appellee's brief on the merits until September 24, 1982.
Sept. 24, 1982	Brief of the United States filed.
Nov. 5, 1982	CIRCULATED.
Dec. 28, 1982	Reply brief for the appellant filed. (D).
Jan. 10, 1983	ARGUED.